The Economist

20010721

PRINT EDITION

Full contents
Enlarge current cover
Past issues/regional covers
Subscribe

GLOBAL AGENDA
POLITICS THIS WEEK
BUSINESS THIS WEEK
OPINION
Leaders
Letters

WORLD
United States
The Americas
Asia
Middle East & Africa
Europe
Britain
Country Briefings
Cities Guide

SURVEYS

BUSINESS
Management Reading
Business Education
Executive Dialogue

FINANCE & ECONOMICS
Economics Focus
Economics A-Z

SCIENCE & TECHNOLOGY
Technology Quarterly

PEOPLE
Obituary

BOOKS & ARTS
Style Guide

MARKETS & DATA
Weekly Indicators
Currencies
Big Mac Index

DIVERSIONS

RESEARCH TOOLS

CLASSIFIEDS

DELIVERY OPTIONS
E-mail Newsletters
Mobile Edition
RSS Feeds

ONLINE FEATURES
Cities Guide Go
Country Briefings Go
Audio interviews Go
Classifieds Go

The Economist Group
Economist Intelligence Unit
Economist Conferences
The World In
Intelligent Life
CFO
Roll Call
European Voice
EuroFinance Conferences
Economist Diaries and Business Gifts

Print Edition July 21st 2001

What are they really for?
George Bush needs to come clean about his missile-defence ambitions ... More on this week's lead article

The world this week

Business this week
Politics this week

Leaders

Missile defences
What are they really for?

Sanctions policy
Stop helping Fidel and Saddam

India and Pakistan
Hope among the ruins

France
Liberty, equality, impunity?

Climate change
Life after Kyoto

Britain's Conservatives
It has to be Ken

Letters

On wealth, Mexico and America, Virgin Rail, idolatory

Special

Emerging markets
How the bug can spread

United States

The Democrats
More questions than answers

Public life in Arkansas
Murder, rape and Clinton-bashing

Missile tests
If at first you don't succeed...

California's power crisis
How to keep the fans turning

Lexington
The incredible shrinking VP

The Americas

Argentina's economic crisis
Austerity, or bust

Tourism in Peru
Road to ruin

Mexico's foreign policy
Branching out

Rebuilding El Salvador
Homeless, and increasingly hopeless

Asia

India and Pakistan
Summit ascended, but Kashmir not yet broached

Russia and China
Remaking history

China's pollution
Exposing a dirty secret

Indonesia
Who's in charge?

Piracy in Asia
Dangerous waters

Japanese reform
Sinking, not flying

Previous print editions

Jul 14th 2001
Jul 7th 2001
Jun 30th 2001
Jun 23rd 2001
Jun 16th 2001

More print editions and covers »

Subscribe

Subscribe to the print edition
Or buy a Web subscription for full access online
RSS feeds
Receive this page by RSS feed

Surveys

Putin's choice
Good in part
A reconditioned model
States within the state
Mystery man
Waiting for the crunch
Endangered species
In search of an identity
Sources and acknowledgements
Offer to readers

Business

The technology industry
Big is beautiful again

Computing
Revenge of the dinosaurs

Swissair
A scary Swiss meltdown

Black empowerment
Skin deep

Iranian privatisation
A mess

Management consultants
Winners' curse

Drugs
Marketing madness

Face value
The unknown media mogul

Finance & Economics

Mortgage-lending agencies in America
Big scary monsters

The American economy
Greenspan's glimmer

German finance
Penny bazaar

Indian mutual funds
Unit what?

Pampering staff
Elf help

French banking
Farmers unite

Economics focus
Frédéric Bastiat

Science & Technology

Climate change
Kyoto's last stand

Hydrogen-powered cars
Replacing gas with a gas

Advertisement

International

Israeli-Palestinian fighting
Prospects of war

Egyptian unemployment
Summer of fury

African unity
Gadfly Qaddafi

Burundi
Doubtful peace

Europe

Greece's threatened reforms
A need to clear the air

Portugal's politics
Guterres stumbles

Italy's finances
Rocky road ahead

Europe's single currency
Trust or mistrust thy euro neighbour?

German gays
Stronger-wristed

France's secret service(s)
Letters of cachet

Divided Cyprus
The danger of over-doggedness

Bulgaria's royal prime minister
The wrong job?

Charlemagne
Juan Jose Ibarretxe

Britain

Medical negligence
Tragic flaws

Leadership election
The battle for the Tory party

Tory homophobia
To fall like Lucifer

Nightlife
Old school tie

Gambling
Paris, Nevada; Luxor, Lancashire

Transport strategy
Going nowhere

Bagehot
Robin Cook's revenge

Lord Archer
A taste for fiction

Articles flagged with this icon are printed only in the British edition of *The Economist*

The origins of malaria
Following the plough

Bacteria and ore-formation
Goldbugs

Books & Arts

Air travel
The way we fly now

A philosopher's letters
Love, Bertie

Summer movies
Hothouse flowers

Archaeology
Digging for truth

Simone Weil and Rosa Parks
Two kinds of heroism

Daniel Ellsberg
Treachery, egotism or bravery?

New fiction
Not amused

Immigration
No entry

Correction

Obituary

Katharine Graham

Economic and Financial Indicators

Money and interest rates

Oil reserves

Commodity price index

Stockmarkets

Trade, exchange rates and budgets

The world's biggest companies

Overview

Output, demand and jobs

Prices and wages

Emerging-Market Indicators

The Economist poll of forecasters

Overview

Economy

Financial markets

Advertisement

Classifieds

Jobs
Account Executive - Mid Atlantic Enterprise Sales
The Mid-Atlantic Account Executive key objective is to maximize s....

Business / Consumer
WSI Internet - Start Your Own Business
Business Opportunity - WSI Internet Start Your Own Busines....

Tenders
Expression of Interest - Management Audit
Expression of Interest Management Audit Consultation Company The Tim....

Jobs
Associate Professor in International Relations/EU External Relations
Universiteit Maastricht (UM) is renowned f....

Tenders
Request for Proposals: A course on Budget Policies and Investments for Children
Request for Proposals: ....

Jobs
Director - Energy, Environment & Water Research Center (EEWRC)
The Cyprus Institute (CyI) recruits the Di....

Sponsors' feature

About sponsorship »

Copyright © The Economist Newspaper Limited 2006. All rights reserved. Advertising Info | Legal disclaimer | Accessibility | Privacy policy | Terms & Conditions | Help

Produced by = ECO PDF TEAM =
Thanks xxmama

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Business this week

Jul 19th 2001
From The Economist print edition

American woes

Alan Greenspan, chairman of the Federal Reserve, downplayed the chances of a fast recovery for America's slowing economy. He said that he hoped that the economy had hit the bottom; but he acknowledged that it was not yet free of risk, leaving the door open for possible further interest-rate cuts.

See article: Greenspan's glimmer

Economic indicators left uncertain the hopes that an American recovery was on the cards. **Industrial production** fell in June for the ninth month in succession to 3.6% lower than a year ago. Inflation was also on the up. The consumer-price index edged up in June to 3.2% over a year earlier.

US company results
Second quarter net profit/loss, $bn

	2000	2001
Ford Motor	1.51	-0.75
AOL Time Warner	-0.92	-0.73
Intel	3.14	0.20
J.P. Morgan Chase	1.63	0.38
General Motors	1.75	0.48
Merrill Lynch	0.92	0.54
Boeing	0.62	0.84
Coca-Cola	0.93	1.12
IBM	1.94	2.05
Citigroup	3.34	3.54

Sources: Company reports; Reuters

Mr Greenspan's less than optimistic prognosis for the economy was also backed up by a slew of **company results**, most of which were bad.

Profits at **Intel**, the world's biggest chip maker, nose-dived by 94% in the second quarter to $200m, as the slowing economy hit PC sales and sparked a price war. The company tried to cheer investors with the information that business was unlikely to deteriorate in the next quarter.

Second-quarter losses at **Ford** hit $752m, partly because of an expensive recall of vehicles fitted with suspect Bridgestone tyres. **General Motors** fared better. It made profits of $477m over the same period, down only 73% from the year before. However, **Boeing**, an aerospace giant, announced that profits were up by 35% at $840m.

America's slumping markets and nervous investors took their toll on **Merrill Lynch**, America's biggest stockbroker. It announced that second-quarter profits were down 41% from a year ago. **Charles Schwab**, America's biggest online stockbroker, said that profits had fallen by 26% in the same period.

J.P. Morgan Chase proved that investment banking is not as lucrative as it once was. Profits for its latest quarter were down by 68% to $378m. Job cuts seem likely to follow.

American Express, an American credit-card and travellers-cheque firm, gave a warning that profits for the second quarter would be down by around 76%. It added that prospects for the rest of this year and next looked gloomy; it will lay off up to 5,000 staff.

Turkey's lira hit a fresh low against the dollar, even after the government raised short-term interest rates. The lira is now down by over 50% since the start of the year. The Turkish economy minister, Kemal Dervis, had one bit of good news: the communications minister, a constant thorn in his side, resigned. But the risks of a debt default persist.

See article: How the bug can spread

Chips with everything

Sanmina, an American electronics company, acquired a larger rival, **SCI Systems**, in a deal worth some $4.1 billion in shares. Demand for the outsourced manufacturing that the firms offer, particularly from the mobile-phone and computer industries, had boomed but the technology slump created plenty of spare capacity and further mergers in the industry are expected.

Philips, Europe's leading consumer-electronics firm and third-biggest chip maker, announced second-quarter losses of *euro*770m ($672m) compared with a profit of *euro*3.6 billion last year. Its highly profitable chip business has suffered the same fate as its rivals' and the 4,000 job losses announced are likely to fall heaviest on these operations.

Infineon, Europe's second-biggest chip maker, sold new shares worth *euro*1.5 billion ($1.3 billion) to finance new investment and pay off some debt. The company, controlled by Siemens, a German electronics giant, issued a profit warning in June. World chip demand still languishes.

Software that allows the running of Java programs will not be included in **Microsoft**'s new operating system, Windows XP, or its new browser, for "business reasons". **Sun Microsystems**, Java's creator, was a key hostile witness in Microsoft's antitrust trial.

Chinese expansion

China's economy grew by 7.8% in the second quarter compared with a year ago, according to carefully prepared figures from its government. Some noted that China's growth has barely strayed from this impressive rate for several years.

Inflation in the **euro-zone** dropped to 3% in the year to June from an eight-year high of 3.4% the month before. The European Commission predicted that inflation would slip below the European Central Bank's 2% ceiling early next year.

Pump priming

BP, a British oil giant, agreed to acquire **Veba Oil** from E.ON, a German utility, thereby becoming Germany's largest petrol retailer. The deal—BP will hand over its stake in Ruhrgas, Europe's biggest natural gas distributor, and some money—will be completed next year and value Veba at around *euro*6.5 billion ($5.5 billion), according to E.ON.

Electricité de France and **Fiat** upped their joint bid for **Montedison** so as to sweeten the deal for the shareholders who own the 48% of the big Italian power company outside the grasp of the two bidders. EDF had already allayed the concerns of Italian regulators by restricting its voting rights. The European Commission may yet get involved.

In the bank

Bankgesellschaft Berlin reported losses of a whopping *euro*1.65 billion ($1.52 billion) in 2000 after provisions to cover high-risk property ventures. The bank, controlled by Berlin's city government, said it would raise *euro*2 billion for a recapitalisation. Berlin's government may have to dig into its pockets.

Royal Bank of Scotland, Britain's second-largest bank, raised £2 billion ($2.8 billion) from shareholders to finance the purchase of **Mellon Financial**, an American retail bank. It will chip in £500m of its own cash.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Politics this week

Jul 19th 2001
From The Economist print edition

At the summits

A much-trumpeted meeting between India's prime minister and Pakistan's president ended in deadlock after India refused to discuss the disputed territory of **Kashmir**. But at least the leaders of the two nuclear powers agreed to meet again for talks later this year.

See article: Summit ascended, but Kashmir not yet broached

The heads of government of the leading industrial countries and Russia headed for Genoa for the **Group of Eight** meeting. So did anarchists, greens, anti-capitalists, Italian Catholics and sundry loonies.

Lesser lights will head for Bonn, in Germany, for a big **environmental summit** to discuss the Kyoto Protocol. The Europeans want to revive the ailing UN treaty on global warming. Others are less keen: President George Bush has called it "fatally flawed"; the Japanese are sitting on the fence.

See article: Kyoto's last stand

Israeli tanks and infantry advanced threateningly in the occupied territories after a suicide-bomb exploded in **Israel**. While militants pressed for all-out war, Ariel Sharon and Yasser Arafat struggled to keep their tense confrontation within limits.

See article: Prospects of war

Supporters of **George Bush**'s controversial missile-defence plan claimed a victory when a prototype system successfully shot down a dummy rocket over the Pacific Ocean. Previous attempts had failed.

See article: If at first you don't succeed...

Emerging slowly

Argentina's government, beset by worries that it would default on its debts, claimed to have gained the backing both of its own supporters and of provincial governors from the opposition Peronists for public-spending cuts aimed at balancing the budget this year and next. But investors were sceptical: Argentine shares and bonds fell back after a brief rally.

See article: Austerity, or bust

Popularity contests

The popularity of Japan's prime minister, **Junichiro Koizumi**, slipped from 80% to 67% according to an opinion poll, but his ruling coalition looked set to keep its majority in parliament's upper-house election on July 29th.

Britain's opposition Conservative members of Parliament voted to offer their rank-and-file a stark choice in the election of a new party leader: either a little-

known Eurosceptic, Iain Duncan Smith, or a Europhile, Kenneth Clarke, a former chancellor of the exchequer. The election, open to all party members, takes place in September.

See article: The battle for the Tory party

Sheep and wolves

Four officials at the United Nation's criminal tribunal for **Rwanda** have been found to be suspects in the 1994 genocide they were supposed to be investigating. Their contracts have not been renewed. Three other suspects were arrested in the Netherlands, Switzerland and Belgium.

Rebels and the government in **Sierra Leone** have agreed to stop diamond mining in the eastern region to help disarmament proceed and allow the deployment of UN peacekeepers.

Legal immigrants?

During a visit to America, President Vicente Fox of **Mexico** called for an amnesty for 3m Mexican illegals north of the border. The Bush administration is considering giving permanent legal residency to them but the plan faces strong opposition from conservative Republicans in Congress.

See article: Branching out

A personal secretary of Silvio Berlusconi, **Italy**'s new prime minister, was sentenced to 2 1/2 years in prison for trying to cover up evidence in a tax-police bribery case involving one of the great man's companies.

Macedonia's government complained publicly of the terms NATO countries want it to offer its ethnic-Albanian rebels. Too soft by half, it said.

Myanmar's government freed 11 more political prisoners. But there are still 1,800 to go.

Lord Archer, a former deputy chairman of the Conservative Party and a successful novelist, was sentenced to four years in prison for perjury and perverting the course of justice in his libel case against the *Daily Star* in 1987.

See article: A taste for fiction

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Missile defences

What are they really for?

Jul 19th 2001
From The Economist print edition

George Bush needs to come clean about his missile-defence ambitions

FOR those who thought the cold war, and with it the risk of nuclear annihilation, had ended over ten years ago, there is something a bit disturbing about the signals that the two main nuclear powers have exchanged over the past week. The United States has told Russia that it may soon bust the Anti-Ballistic Missile (ABM) Treaty; the Kremlin, therefore, had better negotiate some new regime or else see that treaty, and with it all hope of privileged strategic relations with America, tossed in the dustbin. Russia has been squealing in protest at America's successful, but not in itself very important, test of an anti-missile system on July 14th. And it has sulkily reminded America that tearing up the ABM treaty could mean forfeiting many other arms-control arrangements.

What's more—as the leaders of Russia and China implicitly suggested this week by sealing a strategic partnership—unilateral action by America could force Russia and China into an ever-closer embrace: a deadly combination, in other words, of Russia's know-how and China's assertiveness. We are not impressed, American officials retort: you Russians and Chinese need us more than you need each other, and your interests do not coincide. Moreover, regardless of what we do, Russia will have to cut its long-range nuclear force, while China will anyway increase its arsenal; so stop trying to influence our plans with empty threats. These plans, says the Pentagon, include the development of a wide range of anti-missile defences based on land, sea, air and perhaps space.

Even if the tone of this geopolitical poker game sounds troubling, things may not be as bad as they appear. After all, the background to the entire contest is America's unmatched combination of economic and military power. That means it can offer incentives, and issue warnings, with far greater credibility than anybody else.

And the prizes in the game certainly look attractive. If its negotiating strategy works, America will give itself a free hand to fend off missile attacks from smaller, emerging nuclear powers while keeping Russia content. But for America to win the game, it will not be enough simply to play its own—admittedly, strong—cards and fold its arms. Partly because America is a democracy, and aspires to lead a coalition of democracies, its chances of success will also depend on winning a moral argument, and convincing people that it is acting in good faith. It will lose out if it appears to be gambling with international peace for the sake of extending a world hegemony that is already beyond question. It will prevail only if it can persuade the world that busting the ABM treaty is a means to security, not an end in itself.

Ever wilder wildcats

How, then, can the United States win the moral contest? Partly through the case it chooses to make. There are some good arguments for developing anti-missile defences, free from existing treaty constraints, and some bad ones. The best argument is also the simplest: the ABM treaty was designed for a bipolar world—not for today, when the capacity to build rockets, and tip them with deadly warheads, is spreading fast. Nobody can deny that such rockets pose a threat: they did even in 1991, when Iraq fired Scud missiles at American bases and the cities of Israel. But the danger is primarily to American bases abroad and to the territory of allies, not the American homeland; and the type of defences needed to cope with that danger need not breach the ABM agreement.

Yet, even if there is little threat to the American homeland now, is it not likely that one will emerge soon, as the range of rockets deployed by countries like North Korea and Iran grows longer? And to cope with those dangers, is it not desirable to tear up the ABM treaty as soon as possible?

To this argument, the sceptic will retort that no rogue with rockets, however incorrigible, would dare attack America and risk annihilation. The ABM-buster, in turn, will respond that rogues are curious folk who may not be deterred by threats of devastation. Neither viewpoint is entirely convincing.

A case for defending America against limited missile strikes can certainly be made, but it is a subtle, nuanced one. Although the launching of “suicide strikes” on American soil by some eccentric tyrant may be unlikely, his mere ability to threaten, say, Los Angeles would influence the tone of any stand-off between him and the United States. So would America’s ability to intercept his rockets. This ability to stop wildcat missiles in their tracks would thus be a kind of reinsurance policy—combined with other ways of keeping the missile threat in check, including diplomacy and deterrence.

That beguiling astrodome

So far, so good. But it is not self-evident that the development of limited anti-missile defences requires the busting of the ABM treaty “within months”. Such talk may help to put pressure on Russia, but it also fuels the suspicion that scrapping the treaty is an end, not a means. And in the wake of this suspicion comes another: that “limited” anti-missile defences are merely a stalking-horse for the construction of a giant shield over the whole of America. That is a chimera, technically probably impossible to achieve and strategically highly dangerous, because it would threaten the entire structure of arms control that, whatever its shortcomings, is still the world’s best hope of containing the most dangerous weapons.

The idea of anti-missile defence as a partial breastplate—assuming it can be had at reasonable financial and diplomatic cost—may not be as alluring as that of an “astrodome” under which all Americans could hunker. But America’s hopes of a moral victory in the geopolitical poker game must rest on preferring honest arguments—and ultimately honest policy choices—over specious ones. That means explicitly forswearing any astrodome defence, and at the same time working energetically to cut nuclear weapons and to seek stability through international agreements, not least to prevent the militarisation of space. If Mr Bush could openly dedicate himself to these goals, he would find that much of the hostility to his missile-defence plans would disappear.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Sanctions policy

Stop helping Fidel and Saddam

Jul 19th 2001
From The Economist print edition

The case for thinking again about America's sanctions

AP

"I WOULD encourage Congress to stop for a while. I mean, stop, look, and listen before you impose a sanction." Thus Colin Powell, America's secretary of state, during his confirmation hearings at the start of the year. It is hard to think of any policy that is more counter-productive than America's approach to sanctions. However, even if the United States deliberately wants to aid dictators like Fidel Castro while irritating its allies—which is what it achieves, on the evidence so far, by its persistence with sanctions—it would do well to make the policy a little more selective, and clearer.

George Bush came to office pledging to simplify and reduce America's use of sanctions. He has not succeeded. Dozens of bills threatening sanctions for everything from weapons-proliferation to money-laundering, and at least one calling for more sanctions, are being considered by Congress. The House of Representatives seems set to renew the Iran-Libya Sanctions Act, a law that imposes sanctions on foreign companies that do business in those two countries.

True, on July 16th Mr Bush decided not to activate Title III of the Helms-Burton act, which would allow American companies and individuals to sue foreign ones that use property seized by the Castro government. Yet he has left in place a trade embargo, endless constraints on foreigners who do business with Cuba (a bona fide member of the World Trade Organisation), and limits on the amount of cash Cuban-Americans can send to relations on the island, a restriction that has just been reinforced.

Indeed, the main arguments against sanctions are illustrated by their role in propping up Mr Castro. They have provided the dictator with a convenient excuse for all that is wrong with his country. They are also woefully indiscriminate weapons: plenty of poor Cubans, not to mention perfectly respectable foreign business people, have suffered needlessly. And sanctions are as difficult to get rid of as they are easy to invent, since giving up sanctions nearly always involves a climbdown by the sanctioner. If Mr Bush gave up the embargo, Mr Castro would claim victory.

Look at the evidence

Imposing restrictions on particular sorts of trade has sometimes worked. The United Nations arms embargo on Saddam Hussein, which has slowed his nuclear ambitions, is one example. Yet, as Iraq also illustrates, wider sanctions can have horrific consequences when they are twisted by callous dictators against their own people—Iraqi infant mortality has risen by 160% since 1991, though only in the areas where Mr Hussein controls the distribution of food and medicine. And, as in Yugoslavia, sanctions in Iraq have increased local corruption by making legitimate trade so difficult.

None of this suggests that sanctions should be altogether banned. Apart from anything else, they are one of the few diplomatic threats, short of war, that the democracies can wield against the Saddams and Milosevics of this world. The sporting sanctions against apartheid South Africa certainly (and properly) caused the ruling white minority considerable pain. There is a case for making America's current ones "smarter" as well. But the woeful overall track-record of sanctions surely demands that they be used sparingly, and not as some default option, as many congressmen seem to think.

Besides, with America's sanctions there is an added injustice: their extra-territoriality. Impose restrictions on your own companies and people if you want to. But Helms-Burton also mauls non-Americans—for instance, banning directors of companies that have bought Cuban assets from visiting the United States (including a former editor of this newspaper). Under the Iran-Libya act, the president can choose to bar any foreign firm investing more than $20m in the Iranian or Libyan oil industry from selling goods in America or receiving big loans from American banks. But would supporters of such measures applaud if Europe decided to do just the same, hammering American firms and barring their CEOs from Paris because it dislikes Mr Bush's policy on global warming?

The Cuban embargo has helped Mr Castro to outlast nine American presidents. Who knows what invidious records the other embargoes might yet help to achieve. Mr Powell's instinct was correct: it is time to stop and think.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

India and Pakistan

Hope among the ruins

Jul 19th 2001
From The Economist print edition

The India-Pakistan summit in Agra looked like a disaster. It wasn't

THERE is an old saying among diplomats that "nothing is agreed until everything is agreed," which is why, despite all the goodwill and optimism at the start of last weekend's Indo-Pakistani summit, the ending came with recrimination, deadlock and a midnight dash for the airport (see article). Pervez Musharraf, Pakistan's self-appointed president, and Atal Behari Vajpayee, India's prime minister, could not agree on any form of joint statement, or even to hold a press conference explaining what had gone wrong.

What had gone wrong, of course, was Kashmir. Had a way been found to fudge the Kashmir issue, much else was ready to be approved: joint action on narcotics, confidence-building measures to reduce tension between the two nuclear-equipped military establishments, oil pipelines, trade and, most important of all, regular annual summits, six-monthly foreign ministers' meetings and a host of the lesser official dialogues that form the normal framework for intercourse between neighbours who are not enemies. But Kashmir, as had always seemed likely, held all else hostage.

On this issue, it is difficult for either side to make any form of concession. In many Indian minds, talk of autonomy, let alone independence, for Kashmir threatens the much wider unravelling of the country. For Pakistan, riddled as it is with tens if not hundreds of thousands of well-armed Islamic militants for whom the Kashmiri *jihad* is a sacred cause, any hint of backsliding is dangerous. Mr Vajpayee heads a coalition government and faces strong opposition to compromise from hardliners within his own Hindu-nationalist party. General Musharraf may not have a coalition to worry about, but he certainly has two powerful and in practice not entirely distinct groups to keep on the right side of: his own fellow-officers, and the *jihadis*, who even before they heard of the collapse of the summit were threatening a return to war. That is why both sides often seem so determined to delimit the outcome of any negotiating procedure before they even begin it.

After the Agra meeting, can there be any picking up of the pieces? Two good consequences, at least, may have emerged from the summit. The first is that, before things got tricky, Mr Vajpayee and General Musharraf had agreed on a return meeting in Islamabad, possibly in December, and that after it collapsed the principle of the visit was reaffirmed. They are also likely to meet in September at the UN General Assembly.

The second is that India was apparently ready to take at least a step towards acknowledging what is obvious to any non-Indian: that Kashmir is a serious obstacle standing in the way of normal relations between the subcontinent's largest countries and that, without progress on it, there cannot be much progress on anything else. This would have constituted a big shift. India's previous formulation, dating back to the Lahore summit of 1999, was to treat Kashmir as simply one of a large range of questions for the two countries to discuss. To Pakistan, that is problematic. What it fears, reasonably, is that India would scoop up all the benefits of a normalised relationship, while continuing to stall on Kashmir. The status quo suits India better than Pakistan since it currently controls most of the state. With the summit deadlocked, the Indian concession is off the table again: but in Agra it was there in principle.

The price of progress

Progress, in any event, seems to have only been on offer at a price. In return for moving closer to an acceptance of the centrality of Kashmir, Mr Vajpayee insisted that Pakistan should agree that the problem of “cross-border terrorism” had to be discussed. These are hard words for any Pakistani president, even a dictatorial one, to accept. To Pakistan the activity of the Kashmiri militants is not terrorism but freedom-fighting: and nor is it “cross-border”, since the “line of control” separating Indian- from Pakistan-held Kashmir is not viewed as a border at all, the militants being Kashmiris fighting in their own land. But on this, his first foray to India since he left it as a child in 1947, General Musharraf needed to buttress his authority at home by standing his ground, so it is entirely possible that at a later meeting a form of words may be found to bridge the gap.

It is true that both sides found it disappointingly hard to resist sounding off in public while the talks were under way, never wise in a sensitive negotiation. But if the two meetings go ahead as planned before the end of the year, and if Pakistan can rein in the militants before they commit the sort of atrocity that would derail the entire enterprise, there is still a chance that the foundations of the Agra summit can be built on.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

France

Liberty, equality, impunity?

Jul 19th 2001
From The Economist print edition

The French president's evasions do not serve France

SOME 340 years—and a revolution—have passed since Louis XIV, equating himself with the state, declared "*L'état, c'est moi*", so why does France's president, Jacques Chirac, still put himself above the laws that apply to ordinary citizens? Why, in particular, has he refused the polite requests of France's magistrates to tell them his side of the stories that have been tarnishing his reputation for the past year? The answer, Mr Chirac explained to the nation on July 14th, the anniversary of the 1789 revolution, is that if he were to meet the judges, he would imperil not himself as a citizen ("I have nothing to hide"), but the office of the presidency, the institutional balance of the republic and even French democracy itself.

Self-serving tosh from a president campaigning to be re-elected next spring? Certainly, the judges could ask some embarrassing questions. For example, when Mr Chirac was mayor of Paris, from 1977 to 1995, and also leader of his party, the Rally for the Republic, did he have a role in financing his own and other parties with kickbacks on public-works contracts? Or did he know about alleged vote-rigging on his behalf? And just why, between 1992 and 1995, did he use cash—allegedly, though Mr Chirac calls the figures absurd, to the tune of over $450,000 at the then exchange rates—to pay for airline tickets and hotel bills for himself, his family and his entourage? Was it really for reasons of security? And did the money really come from secret, though perfectly legal, funds accumulated during his final stint as prime minister, from 1986 to 1988, or did it come from corporate kickbacks a bit later?

It is possible, of course, that Mr Chirac's reluctance to answer such questions from the judges is indeed driven by an altruistic concern for the greater good. After all, a round of judicial interrogations could turn out to be a prolonged distraction from the affairs of state. Moreover, why should he submit to the indignity? The constitution gives an incumbent president immunity from prosecution for any crime other than treason, regardless of when the crime was committed. It is arguable—in the past month two judicial authorities have contradicted one another—that the immunity extends even to appearing as a witness. And perhaps Mr Chirac is indeed, as he claimed last December, "the permanent victim" of a sustained conspiracy of slander and lies.

A matter of tradition

The president may well have behaved no worse than others before him. The habit of delivering secret funds, taken in cash each month from the Bank of France to the presidential palace and the prime minister's office, dates back to 1946; the sums involved nowadays amount to some $50m a year. By dipping into them the president was only following what he calls "a tradition". Moreover, most of the supposed scandals date back to an era when political parties did not enjoy public subsidies and so were hard-pressed to finance their campaigns. In other words, is there any point in raking up the past? Most French voters viewed with horror the judicial torture of Bill Clinton, another western president whose problems began with a distant financial scandal.

Unfortunately, these arguments contain two flaws. One is that Mr Chirac's concern to protect the republic's institutions paradoxically weakens them. Forget the immunity-conferring niceties of Article 68 of the constitution, interpreted in Mr Chirac's favour by a Constitutional Council whose then president, Roland Dumas, is himself now appealing against a jail sentence for corruption. The fact is that if one

citizen is above the law while others are not, it erodes popular confidence in democratic equality and political accountability. In the end, presidency, parliament and judiciary are all discredited.

But times change

The second flaw is the reluctance to recognise that France is changing faster than its politicians. Mr Chirac has been in politics for almost 40 years, serving the taxpayers but also, at their expense, being dined, wined and lodged in a splendour that most can barely imagine. So, too, the other leading politicians of his and earlier generations. It is a quirk of timing that he should face the scrutiny of a judiciary that so studiously ignored his predecessors.

Actually, not quite a quirk. With hindsight, Mr Chirac should recognise the scrutiny as inevitable. After all, he was the president who in 1996 initiated the reform that has loosened governmental control over France's judges. Meanwhile, membership of the European Union, with its single market, is ending the mutual cronyism of France's business and political elites: EU regulators and foreign investors alike demand openness, not secrecy. France's politicians now have to accept what this implies. At the least it means, as the prime minister has promised, redrawing the rules on presidential immunity. It also means doing away with the secret funds: it is banana-republic stuff to be handing out to ministers and their aides wads of cash that will never be declared to the taxman.

Most of all, it means adopting the reflex of openness in public affairs. Nowhere do politicians in power relish this. In France, the culture in politics and business alike has long been to conceal rather than to reveal. Only last year, for example, did France's corporate bosses agree to publish their salaries, and few French voters would dream of asking from their politicians the personal details—of health and sexual behaviour, say—that Americans view as their right.

The French would be right to say that sexual behaviour should usually be regarded as private. But financial matters are different, especially where bribes, conflicts of interest or taxpayers' money may be concerned, and that distinction is starting to take hold. It is tempting to view the mesh of scandals trapping so many of the elite as proof that France is irredeemably corrupt. Yet the fact that the scandals are now in the press and before the courts is surely proof to the contrary, evidence rather that France is cleaning up its act. If the politicians, eager to wage a nasty campaign for next spring's presidential and parliamentary elections, try to halt the change, the "permanent victim" will be not Mr Chirac but France itself.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

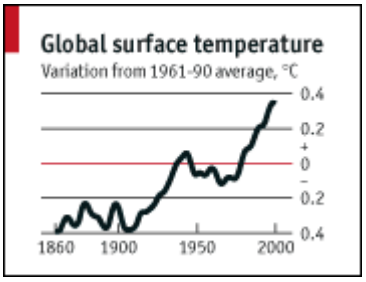
Climate change

Life after Kyoto

Jul 19th 2001
From The Economist print edition

It is time to start work on alternative global mechanisms for dealing with climate change

Get article background



EVEN Stuart Eizenstat, the man who negotiated the Kyoto Protocol, a UN treaty on climate change, on behalf of the Clinton administration, thinks "with great remorse" that the Kyoto treaty is dead. Yet the Europeans do not quite agree.

Instead, they are fighting hard to salvage Kyoto at a big environmental meeting this week and next in Bonn (see article). The treaty was dealt a serious blow a few months ago when George Bush affirmed his strong opposition to it. The EU could still, in theory, ram it into force if Japan now also signs up; but the Japanese are playing coy. So the treaty may well collapse in the coming months—and the Europeans can then join Mr Eizenstat in bidding Kyoto a tearful farewell.

The real question now should be: what ought countries that genuinely care about climate change, as opposed to those that prefer moralistic posturing, to do after the death of Kyoto? European leaders will be tempted simply to throw mud at the United States. Mr Bush indeed deserves much blame for clumsily wrecking a painstakingly negotiated effort to respond to what looks increasingly to be a real threat of global warming. Yet if only acrimony and finger-pointing follow the demise of Kyoto, there will be little chance of any co-operation on any global climate treaty for many years.

That would be a pity, for the best approach to tackling this most global of problems must be through a binding global treaty. To give Mr Bush his due, Kyoto was and remains a badly flawed treaty. Its targets are too ambitious, and its timetable too short; this has made it front-loaded and so needlessly expensive. And although rich countries, which have produced most greenhouse-gas emissions, should act first, Kyoto fails to impose commitments on poor countries, even though within decades India and China will be the biggest emitters.

Kill Kyoto to save it?

Optimists still insist that such flaws in Kyoto could be fixed by sincere negotiators willing to find clever ideas for compromise. The targets could be made more reasonable, and the timetable extended, hugely lowering the costs of complying with the treaty, and also making it easier to win a promise of action by poor countries. Sadly, the Kyoto process has not been blessed with much sincerity or cleverness: the Americans have been lacking in the first, and the Europeans woefully inadequate in the second. The resultant bitterness goes a long way to explaining why Kyoto has in effect reached a dead end, whatever Japan eventually decides.

The Europeans' response to this now seems likely to be to thumb their noses at the Yanks and go ahead and implement a high-minded, "European" version of Kyoto. Their idea is that, as with some earlier free-trade deals, their good example will eventually lure the Americans back on board. But the trade analogy does not hold: freer trade is of greatest benefit to the liberaliser itself, whereas Kyoto imposes costs, giving non-participants all the advantages of free riders. Moreover, if the Europeans do indeed proceed with an inflexible implementation of Kyoto, they will make it even less likely that an American administration will ever join a global climate pact.

The best hope for action on climate change may lie neither in fussing for months to produce a rump

Kyoto Protocol, nor in its partial implementation by Europe on its own; but, rather, in hastening its demise. Then countries that are serious can forge ahead with trading schemes, carbon taxes and the like on a domestic or regional level. Europeans, for example, could continue with their plans for an EU-wide carbon-trading scheme—and even keep to their Kyoto targets if they can persuade European industry that it will not thereby be unfairly burdened. Mr Bush, similarly, could put his recently mooted notion of a North American emissions-trading regime to the test, though he would have to accept some mandatory targets (which he has so far rejected) to make it work.

Those countries that do nothing of substance will then be shamed to be shown up as hypocrites. And, once the dust from Kyoto has settled, all countries can then try again to agree a treaty which is binding in its targets yet flexible in its mechanisms, is long-term in scope, adapts as science and technology improves, and includes poor countries. It would be worth the delay of a few years to get a treaty that America could embrace. Climate change will be with us for at least a century. It will need a solution large enough and durable enough to last at least that long.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Britain's Conservatives

It has to be Ken

Jul 19th 2001
From The Economist print edition

But Kenneth Clarke still needs to reassure Tories on Europe

Get article background

A FOREIGNER could be forgiven for wondering why on earth Britons seem so interested in the interminable efforts of an opposition party to choose a new leader, especially since the said party has been crushed by Tony Blair in two general elections, and has long looked unable to be led out of a paper bag. Moreover, that foreigner might say, Britain's Conservative Party is most divided about whether or not it likes foreigners—at least European ones—so why not ignore it until it grows up? Yet that is precisely the point. The Tories' leadership contest is playing out, in slow motion, the party's fundamental divide over relations with the European Union. And since that divide has echoes in the country as a whole—maddeningly xenophobic one moment, the epitome of globalisation the next—it is well worth watching.

This week Tory members of parliament narrowed the leadership candidates down to two, between whom the 300,000 ordinary party members will choose in mid-September (see article). The choice is stark: between Kenneth Clarke, the paunchy, plain-speaking, mine's-a-pint man of great ministerial experience and with strong views in favour of Britain joining the European single currency; and Iain Duncan Smith, the upright former soldier with no ministerial experience, in favour of capital and corporal punishment, and with strong views against Britain joining the euro. Both men say they will work with the other if they lose. But the chance of a split in the party must be far from negligible.

So which should the Tory members choose? Above all, they need someone who can make their party look like a viable government, who can give Mr Blair a mauling, who will have the flexibility to keep the party united, and who can still leave them feeling good about being Conservatives.

Our choice, arising both from our selfish, non-party-political views and from a sense of what could be best for the Tories, would be Mr Clarke. Although Mr Duncan Smith's inexperience should make little difference (he could learn), his inflexibility must count against him. In office, he could doubtless soften his stance on hanging and flogging. But his position on the euro is immutable: he is against joining in principle, whatever the situation, whatever the state of the EU, now and for ever. This makes too much of a mere currency arrangement. But also he would be a double-or-quits choice for the Tories: if, in a referendum, Britons were to vote to join he would either have to quit as leader, recant, or declare that he would campaign henceforth for withdrawal. Tactically, to choose a never-man would be madness.

Yet Mr Clarke, too, has problems on Europe. His great virtue in other policies is that he combines intelligence and a sense of principle with pragmatism. On the euro, however, he sounds like a priest. To succeed, he will have to do two things. One will be to emphasise that although he favours joining it, the euro is not the be-all and end-all of his political life. The second will be to recognise that there are wider reasons, beyond the euro, why Tories—and indeed the general public—distrust the EU. Tories fear, with Lady Thatcher, that having defeated socialism at home the EU will restore socialism through the backdoor. Mr Clarke must respond to that worry, showing that he realises that Europe does have a bearing on other policy positions, and that he has ideas of his own for a constitutional framework for the EU in which Britain—and especially Tories—could feel at home.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Letters

Jul 19th 2001
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

The wealth effect

SIR – In your survey of the new rich (June 16th) you make an often overlooked point; personal wealth frequently brings with it problems that require careful handling if affluence is not to become a curse rather than a comfort. However, you omit an important recent finding from a Danish survey of almost 1,000 people who committed suicide. It found that if you suffered from mental illness, being wealthy significantly increased your risk of killing yourself.

The authors suggest richer people with a psychiatric disorder might feel more stigmatised and ashamed about having a mental illness. However, as seeing a psychotherapist is more of an acceptable lifestyle choice for the wealthy rather than the poor, the finding is even more puzzling. Another possibility derives from the psychological theory that explanations most accessible to us to account for our predicaments are vital determinants of our morale. Not having money is an extremely convenient explanation for most of us about why we are not as content as we would like. But the wealthy are forced to conclude that their unhappiness might be more difficult to solve than merely pursuing the next pay rise.

Perhaps the reason we stubbornly refuse to see that money is not the solution to all our problems is that this would deeply threaten the rationale underlying most of our busy lives. Paradoxically, it could be that economics is delivering us back to the ancient understanding that there is more to life than money.

Dr Raj Persaud
Consultant psychiatrist, The Maudsley Hospital
London

SIR – You miss an established connection between economic inequality and death. Public-health research shows that all people, not just the poor, living in countries with greater income inequality have a shorter life expectancy. Furthermore, a similar relationship has been found for geographical areas within countries, including America.

Although the underlying mechanism behind this correlation is under debate—candidates are psychosocial deprivation, destroyed social cohesion and certain material conditions correlated with macro-inequality—our current knowledge on these matters suggests that economic inequality costs lives.

Magnus Bygren
Stockholm

SIR – You choose to belittle democracy by defining it as a mere set of laws allowing for the defusion of potential social explosions. The spread across classes of economic rights to protection from the miseries brought about by uncontrolled markets you call a “backlash” against economic downturn. Many of democracy’s proponents see this as the defining characteristic of the institution.

All credit for realising that, in periods of economic downturn, “such times also tend to be those when anger about inequality comes to the fore and starts to have political and social consequences.” This being the case, never in the post-war period have western economies needed a recession as desperately as they do now. A period of low growth or contraction may provide the democratising effects of deflation and a re-emergence of the social safety net that we should expect as an essential sign of democracy.

Richard Weigel
Aiea, Hawaii

Gains from trade

SIR – Your article on the border between the United States and Mexico ("Between here and there", July 7th) misses one of the best exchanges taking place between the two countries: the trade of American technology for the traditional Mexican art of being happy under any circumstances. The people living in this new Mexican-American hybrid land will be able to learn from each other how to enjoy life while being highly competitive and tremendously productive, one of the biggest challenges for humankind in the 21st century.

Alfonso Martinez Cearra
Bilbao

Virgin's response

SIR – In your article on Virgin Rail you manage to state the obvious in the most biased and negative way ("Tilting too far", July 14th). Saying that unless we can get more passengers for the west coast mainline that our sums will not add up is a bit like saying that unless the *Financial Times* and *The Economist* get advertising in their journals they will go bust.

The whole point of Virgin Rail's investment in new trains, faster journey times and greater frequencies is to double passenger numbers. It is as much an equation as a calculated risk. Indeed, every other similar investment has proved that journey time and frequency improvements equal passenger growth that can be calculated. This has happened in France, Sweden, Italy, Germany and Japan.

Not one point in Virgin Rail's favour was included in the article:

• You fail to point out that the trains themselves are being delivered on time and to budget, and that they work very well.

• There was no mention of the fact that the recovery from Hatfield for Virgin Rail was exactly on track with our business plan and that we have been compensated by Railtrack for the events of last year.

• There is also a demanding compensation regime in place in respect of the upgrade, which provides Railtrack with considerable incentive to perform.

• There is no analysis of how some of the risk is now out of the project and of the comparisons mentioned above with experience around the world of introducing high-speed high-frequency services.

Finally, the remarkable thing has actually been how robust the business plan to transform franchises has so far proved, through very good contracts and management by Chris Green and his team. We have achieved 40% growth in passengers since we took over and have now exceeded last year's pre-Hatfield levels. Our recent promotions have worked well; CrossCountry passenger volumes are now 4% above what they were before the accident and west coast 1% better.

Virgin's ambitious and visionary plans for its franchises will reap huge benefits in the future, most importantly for our passengers (and, we hope, the company). By 2005, it will be seen as one of the "best things" we ever did.

It is sad that you do not share any of the spirit of that vision. When it suits *The Economist*, it has recently argued that bold risk-taking vision is what is needed in the industry. That has always been our view as well, which is why we are leading from the front.

Sir Richard Branson
London

Political honours

SIR – It is not only in America that politicians are so revered that they have monuments or public works

named in their honour (Lexington, July 7th). The Marshall Islands has renamed the Kwajalein Missile Range. It is now known as the Ronald Reagan Ballistic Missile Defence Test Site at Kwajalein Atoll. The rest of the facility will retain its original name—United States Army Kwajalein Atoll—leaving some leeway for naming other parts of the much-targeted site in honour of other deserving dignitaries.

Espen Ronneberg
Morganville, New Jersey

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com SPECIAL
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Emerging markets

How the bug can spread

Jul 19th 2001
From The Economist print edition

Argentina and Turkey are standing on the brink of financial chaos. Could another emerging-market meltdown be in the making?

ARGENTINA is staring disaster in the face. Last week, the government had to pay 14% on dollar-denominated short-term domestic debt, overnight interest rates hit 300% and the country lost $3 billion-worth of reserves as investors fretted about default, devaluation or both. After a brief respite this week, the financial markets again became nervous as strikers renewed doubts about the government's ability to deliver its draconian plan of spending cuts (see article).

Earlier in the week it had been Turkey's turn to cause the jitters. The lira plummeted to yet another new low against the dollar—it has fallen by over 50% since January. Stocks plunged, bond yields soared and the government failed to complete an auction of domestic debt. Investors returned tentatively to Turkish assets when a nationalist minister opposed to the country's IMF-backed economic recovery plan resigned on July 17th. But fears that the plan is falling apart persist. The spectre of a debt default still looms.

Nor is the trouble confined to Turkey and Argentina. Brazil too has been hit hard. Its currency, the *real*, has fallen by about 25% since the beginning of the year. To stop it slipping further, interest rates have risen, exacerbating the country's debt problem.

The malaise has spread more widely. Currencies and financial markets have slid in countries as distant as South Africa, Poland and Singapore. *The Economist*'s latest poll shows that growth forecasts are being slashed for emerging economies almost everywhere (see chart 1). Not surprisingly, twitchy investors are asking themselves whether a full-blown emerging-markets crisis is in the air. After Mexico in 1994, East Asia in 1997, Russia in 1998 and Brazil in 1999, is another now due?

There are some eerie parallels between 1998 and today. In July three years ago, Russia was facing deep fiscal problems, but it bought itself breathing space on its debt payments through a bond swap. Argentina, also in deep fiscal trouble, bought itself time with a huge bond swap in June this year. By mid-summer 1998, Russia was having trouble selling domestic debt; reserves were falling and overnight interest rates were soaring. Argentina had similar problems last week. In mid-August 1998, Russia was forced to devalue and default on domestic debt. This set off a chain-reaction of panic across the globe. This "contagion" between seemingly unrelated financial markets and assets caused (in President Clinton's words) "the most dangerous financial crisis

for 50 years".

Things are a bit different today. Unlike the Asian economies in 1997 and Russia in 1998, far fewer emerging economies have fixed exchange rates. Markets are also much less leveraged, and hedge funds play a considerably smaller role than they did then. According to Joyce Chang of investment bank J.P. Morgan, hedge funds make up around 10% of emerging debt markets today, compared with 35-40% at the time of the Russian crisis.

On the other hand, America, the world's biggest economy, is no longer booming. In 1998 it was a powerful engine of growth, helping the troubled East Asian economies to export their way out of their difficulties. This year, America has been dangerously close to recession. Industrial production has fallen for nine consecutive months—the longest decline since 1982.

Some old hands are worried. Former Clinton administration officials fret privately that the outlook in emerging markets is grim. Stanley Fischer, number two at the IMF, who played a key role in previous crises, said recently, "We're obviously seeing contagion from Argentina to Brazil, and from day to day other markets are being hit...the last thing anyone should be is complacent."

Others, notably Paul O'Neill, America's Treasury secretary, are less worried. Mr O'Neill, a man who has publicly warned against exaggerating the risks of contagion, this week dismissed fears about risks from Argentina in an interview with *The Economist*. "You think five years from now anyone will remember this?" he asked.

"You think five years from now anyone will remember this?"

According to Mr O'Neill, Argentina's travails are a localised difficulty in a country with a long history of problems. "They've been off and on in trouble for 70 years or more," he said. "They don't have any export industry to speak of at all. And they like it that way. Nobody forced them to be what they are."

Countries with close links to Argentina, particularly Brazil, would be affected, said Mr O'Neill, but he reckoned there was little likelihood of generalised contagion. "There's not the horrific movement [in financial markets] that feels like a wild fire out of control in the desert." Earlier episodes of contagion, he explained, boiled down to a stampede in markets. "Big guys on horses with whips were hoping the stampede would keep going because they were making an enormous amount of money taking advantage of the stampede." Today's markets were more sophisticated. Continuing the colourful metaphors, Mr O'Neill pointed out that "the sheep are not all running for the cliffs". John Taylor, his point man on international issues, is equally sanguine. He recently suggested that, while a number of emerging countries are facing problems at about the same time, there is little evidence of automatic contagion.

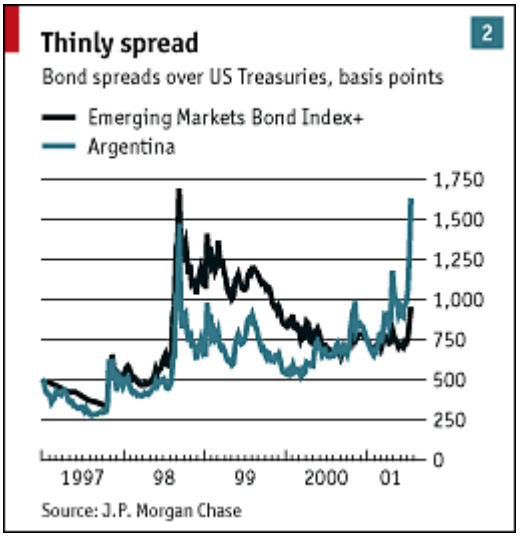
Are America's Treasury officials correct in believing that the risks of contagion today are much smaller than they were in the past, or are they being dangerously complacent? The answer depends on three factors. What will happen in Argentina and Turkey? How will the markets react? And how strong are the emerging economies' defences?

Routes of contagion

Economists reckon that problems can spread among emerging markets through two main channels. The traditional route is via trade links. This was important in East Asia in 1997-98, as about half of emerging Asia's trade was with other countries in Asia. However, neither Argentina nor Turkey is an important market for other emerging economies, so the risk of this sort of contagion is much smaller this time. Brazil's total exports to Argentina account for just over 1% of its GDP.

Far more important is contagion through the financial system—the type that Mr O'Neill was referring to. Trouble in one emerging economy can serve as a "wake-up call" to investors to look more discriminatingly at others with similar problems. Argentina's travails, for instance, are hurting Brazil because they focus attention on Brazil's own large debt burden. Some financial contagion can occur for technical reasons: investors might sell Mexican assets to rebalance their portfolios after losing money in Argentina. Or there can be a generalised panic as investors lose their appetite for risk.

So far, financial contagion from Argentina and Turkey has been limited. Although other countries' currencies and assets have been hit, overall bond spreads (the gap between the interest rate a country pays on its dollar debt and American Treasury bonds) remain well below levels during previous crises (see chart 2). Markets have become much more discriminating than they were three years ago. Exclude Argentina and Turkey, for instance, and spreads on the EMBI index, the benchmark index for emerging markets, have risen by less than 70 basis points (hundredths of a percentage point) since the end of June.



But, of course, neither Argentina nor Turkey has actually defaulted on any debt yet. The panicked reaction in 1998 came in the wake of a chaotic Russian default and devaluation. Much therefore depends on exactly what the crisis countries do. Many analysts reckon Turkey is relatively small fry. If it is forced to default, it may do so only on its domestic debt. Even its external bonds are a fairly small part of the emerging debt markets.

Argentina, in contrast, is a much bigger deal. Its external bonds account for 20% of the most actively traded emerging-market bonds. Add in the possibility of a subsequent default in Brazil, and over a third of all emerging-market bonds would be affected. But here, too, there are several scenarios. Conceivably, Argentina will muddle through and avoid default. The June bond swap together with the recent decision to balance the budget on a cashflow basis means that Argentina may not need more money from the markets this year. Some short-term domestic debt is falling due (the type that precipitated last week's jitters), but there are rumours that the government will arm-twist local banks into swapping maturing short-term debt for one-year bonds.

Short-term relief, however, does not remove Argentina's fundamental problem: its debt has risen to unsustainable levels because its economy has stopped growing. The economy is not growing because low confidence keeps interest rates high, and the peg to a strong dollar erodes competitiveness. That is why many analysts reckon some sort of default is unavoidable. But that, too, could take place in several ways.

Red alert

3

2001 estimates

	Foreign debt as % of exports*	Budget balance as % of GDP†	Short-term debt‡ as % of reserves	Current-account balance as as % of GDP	Exports to US as % of GDP	Real exchange rate§, % change since Jan 1997
China	47	-2.8	11	0.9	4.7	+13
Hong Kong	19	-0.3	11	3.6	28.7	0
Indonesia	186	-4.6	108	2.7	6.0	-43
Malaysia	39	-7.0	20	6.3	23.9	-19
Philippines	108	-3.8	55	9.3	16.1	-32
Singapore	5	1.7	3	21.4	26.2	-8
South Korea	60	-0.4	38	2.8	8.2	-16
Taiwan	24	-6.3	22	3.5	11.2	-14
Thailand	86	-3.0	53	4.7	13.1	-20
Argentina	423	-2.9	96	-3.2	1.0	+15
Brazil	332	-4.7	95	-4.1	2.0	-20
Chile	167	-0.7	44	-2.2	4.4	+4
Colombia	228	-4.4	48	-1.7	10.6	-14
Mexico	93	-0.6	65	-3.6	24.7	+40
Peru	351	-2.2	68	-2.9	3.8	+2
Venezuela	117	-2.7	27	4.7	14.0	+55
South Africa	66	-2.1	268	-0.6	2.6	-10
Turkey	197	-14.5	100	1.7	1.4	+9
Czech Republic	51	-5.2	61	-5.8	2.0	+6
Hungary	87	-2.8	33	-4.4	5.3	+11
Poland	169	-3.6	29	-4.9	0.7	+24
Russia	148	-0.1	39	11.8	3.3	-13

*Goods and services †2000 ‡Disbursed external debt having an original maturity of up to 1 year §J.P. Morgan trade-weighted index

Sources: Economist Intelligence Unit; J.P. Morgan Chase; *The Economist* poll

Figures in red indicate unsustainable levels

Michael Gavin, an economist at UBS Warburg, distinguishes between two default scenarios. An “orderly restructuring” of Argentina’s debt, where politicians remain in control, maintain market confidence and manage a pre-negotiated default, could end up having only a small impact on the debt markets. A chaotic default, where politicians lose control, could end in hyperinflation and a complete shutdown of emerging debt markets. The question is whether such a thing as an “orderly” default is possible.

Taken alone, even the worst case in Argentina is unlikely to shut down emerging debt markets entirely. The biggest risk is that higher spreads and lower confidence force Brazil to default too. And a combined Brazilian and Argentine default could scare remaining investors out of emerging-market debt altogether, and that could cause huge problems for those emerging economies that depend on external finance. Which countries are most at risk?

Weathering the storm

Every big observer of emerging markets, from the IMF to the investment banks, has a model that tries to predict which country is most likely to hit trouble. Most of them use a combination of a number of financial and economic indicators that have proved useful as early warning signals in previous crises.

• **Foreign debt**. What matters is both the level of debt and its rate of increase. Past experience suggests that alarm bells should start ringing once total debt reaches around 200% of exports. On that basis, Brazil, Colombia, Peru, Turkey and Indonesia give cause for concern, while Argentina’s debts of over 420% of exports are frightening. Measured as a share of GDP, rather than exports, Brazil’s debt is bigger than Argentina’s, and this year it has been rising more quickly. At today’s interest rates, Brazil’s situation is unsustainable.

• **Budget deficits.** Hefty government borrowing has often led to a country’s downfall. Turkey’s deficit is expected to rise to almost 15% of GDP this year. Brazil, the Czech Republic, Indonesia, Malaysia and

Taiwan have budget deficits of 5-7% of GDP. Most worrying is Indonesia, where outstanding government debt amounts to 110% of GDP.

• **Short-term borrowing.** Almost as important as the level of debt is its maturity. Countries with excessive short-term foreign debts (of less than 12-months maturity) can suddenly face a liquidity crisis if they cannot roll over existing credits. Short-term debts currently exceed foreign-exchange reserves in Turkey, South Africa and Indonesia. In the rest of East Asia, by contrast, short-term debts have been significantly trimmed since the 1997-98 crisis and reserves have been built up. For instance, the ratio of short-term debt to reserves has fallen in South Korea from over 300% in 1997 to 38% in 2001.

• **Current-account deficits.** The bigger a country's deficit the more new funds it needs to raise each year. Mexico, Brazil, the Czech Republic, Hungary and Poland all have current-account deficits of at least 4% of GDP. In contrast, all the East Asian economies are running current-account surpluses; Russia is also well placed, with a surplus of 10% of GDP.

• **Exchange rates.** Both a country's exchange-rate regime and the level of its currency matter. Countries with pegged exchange rates have fared badly in previous crises, as have those whose currencies had appreciated rapidly and eroded their competitiveness. Pegged to the dollar, the Argentine peso has risen by 15% in real trade-weighted terms since 1997. But even that is less than the 40% rise in the Mexican peso.

Most Asian currencies look super-competitive, but three of them are still pegged to the dollar: China, Hong Kong and Malaysia. The Chinese yuan looks safest, thanks to a current-account surplus and relatively modest external debts. China is also one of the few emerging economies that is expected to remain strong this year, with growth of 7-8%. If Argentina is forced to devalue then the Hong Kong dollar will come under pressure, as it did in 1998. However, speculators will find the Malaysian ringgit a much easier target.

Measured against these criteria, most emerging economies look less vulnerable than they were in 1997-98. In 1997, they had a combined current-account deficit of $70 billion; last year, they ran a surplus of $110 billion. Nonetheless, there are warning signals flashing. Brazil's is red because of its budget deficit and, especially, its debt burden. Mexico has been partially sheltered because its debts are more modest, but the Mexican peso could be riding for a fall. *The Economist*'s Big Mac index suggests that the peso (like its Argentine counterpart) is overvalued relative to other emerging-market currencies. Mexico's current-account deficit has also been widening this year.

Within Europe, Russia is in a comfortable position thanks to a large current-account surplus and broad budget balance. Poland, Hungary and the Czech Republic, in contrast, are more exposed as a result of their big external deficits. A drought of emerging-market funds could hit them hard. East Asian emerging economies are sheltered from an Argentine or Turkish default by their current-account surpluses and lower debt levels. Indonesia, with its larger debts and even larger political worries, is the main exception.

However, the outlook for the rest of East Asia is far from rosy. That is because it is being hit hard by the sharp economic slowdown in America and the global slump in technology. Exports to America account for more than 20% of GDP in Hong Kong, Malaysia and Singapore, and those exports are especially concentrated on IT goods. Singapore is already in recession: its GDP fell at an annual rate of over 10% in the first half of this year. Taiwan has also probably experienced two quarters of declining output. Excluding China, developing Asia is likely to experience its second-slowest year of growth in over two decades. This slump may have little to do with events in Argentina or Turkey, but it is another reason to beware of complacency.

Excluding China, developing Asia is likely to experience its second-slowest year of growth in over two decades

Thanks to the spectre of default from Turkey and/or Argentina, and the prospect of dramatically lower growth in East Asia (China aside) there are few truly bright spots in emerging markets. To be sure, a crash in one country may not cause the kind of generalised panic that it did three years ago. But today the risks may be more insidious. In Latin America, default and the drying up of foreign finance could precipitate a political revolt against liberal economic policies. Continued slump in East Asia could re-expose those countries' domestic financial weaknesses.

But possibly the most serious risk of all is that this would be the first emerging-market crisis to take place while the American economy was also sputtering since Latin America's meltdown in 1982. In that year, recession in America and Europe, together with Latin America's debt crisis, fed upon each other to

give the world economy its worst year since the depression of the 1930s. A prospect, perhaps, to take some of the colour out of Mr O'Neill's cheeks—if not of his metaphors.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The Democrats

More questions than answers

Jul 19th 2001 | INDIANAPOLIS
From The Economist print edition

The Democrats' attempt to find a post-Clinton identity is not going well

FOR a party that at the last election lost all three institutions of government for the first time in 48 years, the future of the Democrats ought to be reasonably bright. Thanks to Jim Jeffords's defection from the Republicans, they already sort-of control the Senate. They are using that power to trumpet favoured policies such as extending the Medicare system to cover prescription drugs, raising the minimum wage, and so on. Unlike other "out" parties, such as the Tories in Britain, the Democrats suffered no landslide, essentially tying the popular vote. And George Bush's polling numbers seem to be drifting slowly down.

Yet to judge by this week's annual meeting of the Democratic Leadership Council in Indianapolis, the party cannot make up its mind how to take advantage of its chances. The meeting was the biggest gathering of elected officials and party members since voting day (700 or so showed up) and the Democrats' first chance to work out lessons from their defeat for the 2002 congressional and the 2004 presidential elections.

The DLC is the modernising wing of the party: pro-business, pro-technology, pro-defence, pro new ideas of every kind. In the past, it has lambasted the left's obsession with narrow interest groups, such as teachers' unions and abortion-rights activists. It has championed welfare reform, free trade, school choice (including vouchers) and even the partial privatisation of Social Security, although by adding private retirement accounts to the system, not by substituting them for it.

With Mr Bush having abandoned school vouchers and with many Democrats lining up to oppose his plans for missile defence, Social Security and trade promotion, the DLC might have used this occasion to remind its colleagues of the centrist message that won Bill Clinton two elections. Instead, the DLC chose to focus not on policies but on a particular electoral group: white male voters.

In the 2000 election, Al Gore won only 36% of the white guys' vote. Democrats did almost as badly in races for the House, Senate and state governors (ie, it wasn't just Mr Gore's enticing personality). Their performance was even more miserable than it looks, because Ross Perot had siphoned off some white males in 1992 and 1996. His Reform Party collapsed in 2000—yet the Democrats did not benefit one jot.

White men account for almost 40% of the current electorate. They account for a high proportion of suburbanites, college-educated people and shareholders—all growing groups (see three panels in our chart) where Mr Bush did well. White men are ideologically more conservative than the population as a whole. Only 16% identify themselves as "liberal" (ie, left wing) compared with 20% of voters in general.

Democrats cannot turn themselves into conservatives. But the New Democrats think they can avoid giving the impression of being the big-government, anti-business party that Mr Gore seemed to trumpet last year. They can also sound (and sometimes be) more conservative on social issues. For example:

• Those who go to church more than once a week voted almost two to one for Mr Bush, a surprising result considering that religious Americans are not a homogeneous group. The DLC answer: support federal funding of social work by churches, synagogues and mosques. Joe Lieberman, Mr Gore's running mate, is preparing his own version of Mr Bush's "faith-based initiative" to bring to the Senate.

• Half of those who voted last time owned guns and two-thirds of them backed Mr Bush. Democrats, say the DLC, need to say explicitly that they support legal gun ownership and the second amendment, rather than talking about tighter gun rules.

• Only 44% of married couples backed Mr Gore (compared with 57% of singles). So the Democrats should be tougher about the sorts of things that worry parents, such as sex and violence on television.

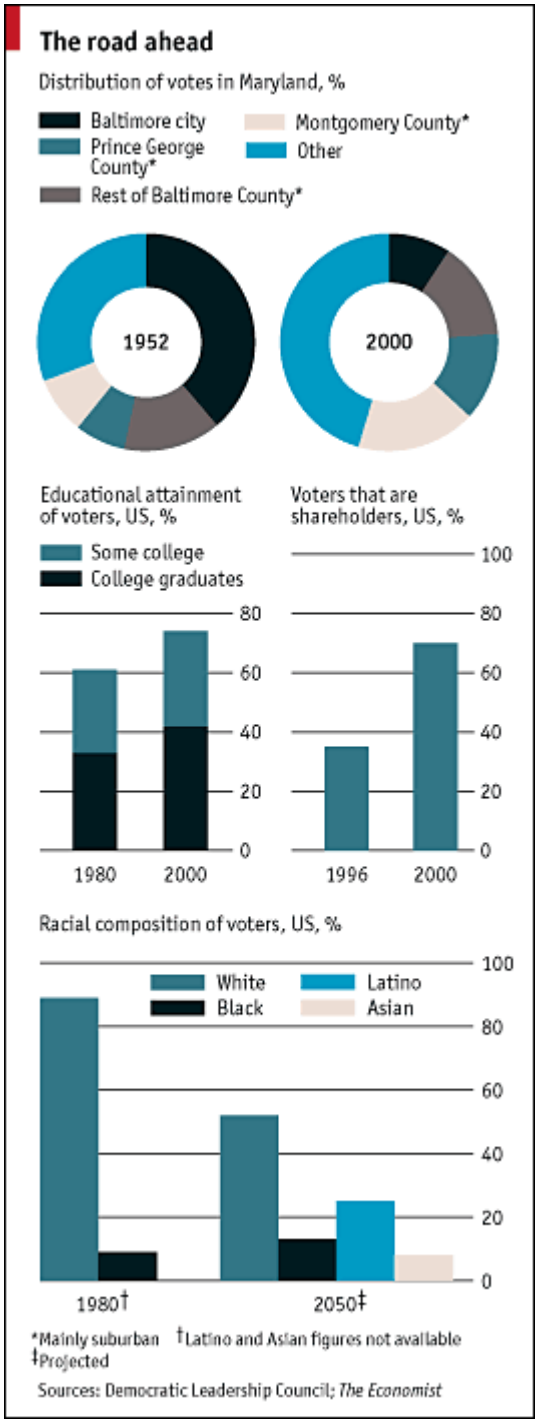
• A huge 64% of military officers say they are Republicans, compared with just 8% who are Democrats—even though Mr Gore supported bigger spending increases for the military than Mr Bush. Answer (in so far as there is one): don't oppose missile defence root and branch; get behind the notion of transforming the military against new threats.

Such an agenda would perhaps make Democrats less off-putting to conservative white men. But does it really represent a winning electoral strategy for Democrats? There are several reasons for doubt.

The first concerns the fourth panel in our chart. The most obvious source of new votes for Democrats in future is not white men but the fast-growing (though under-registered for voting) Latino population who, outside Texas and Florida, vote Democratic by two to one. Even in the short term, this demographic shift could have a massive effect. By one calculation, if whites, blacks and Latinos repeat their 2000 voting patterns in 2004, the Democratic candidate would win.

Parts of the DLC's agenda would no doubt consolidate the Democrats' appeal to Latinos, who hold conservative positions on, say, abortion. Still, that appears to be a secondary consideration. The DLC's primary targets are white males. And even with that group there are problems with its sales pitch.

Mr Gore's failure with white males may have had less to do with "values" than with plain old economics. Middle-income earners did less well during the 1990s than those at the top and, to a lesser extent, the bottom (where people saw their incomes rise for the first time in many years). So it is not certain how much a "values based" appeal will help.



Moreover, there is an exception to the general rule that Democrats did badly among white men. Thanks to a huge get-out-the-vote effort, unions won the industrial heartland states of Michigan and Pennsylvania for Mr Gore. Unions, in other words, have a proven track record in persuading white men to vote Democratic. That has given them increased influence in the party. And they do not think much of the New Democrats' agenda.

Unions disagree with the DLC about trade liberalisation and are far less enthusiastic about the benefits of the new economy. More immediately, they insist that Mr Gore's bashing of Big Oil, Big Insurance and Big Pharma was popular and remains so. Indeed, the Democrats' tactics in Congress are to generate support by attacking Mr Bush's energy plans and by passing health-reform measures opposed by insurance and drugs companies.

It is true that the DLC's new prescriptions—which boil down to moderating the tone on social issues, rather than changing policy positions—could take some of the bitterness out of the Democrats' perennial struggles between left and right. But the essential disagreement remains: unions do not think that populism is poison, as the DLC does, and they see no need for an elaborate agenda to appeal to the values of white men.

"The DLC got mugged by the reality of the 2000 election," crows Robert Borosage of the left-wing

Campaign for America's Future. That is unfair. It was not the DLC that got mugged, but the party as a whole. The Democrats still seem dazed from the assault.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Public life in Arkansas

Murder, rape and Clinton-bashing

Jul 19th 2001 | LITTLE ROCK
From The Economist print edition

In other words, politics as usual in Little Rock

ARKANSAS politics retains the dark Southern-Gothic character of a Flannery O'Connor short story. Wayne DuMond is a case in point. He has just been charged with a woman's murder in Missouri. He is a suspect in another murder case. And he has awkwardly left the governor of Arkansas, Mike Huckabee, with some questions to answer just at the start of a re-election campaign.

AP

DuMond, back in court, back in politics

Mr DuMond is not a particularly sympathetic figure. In 1972 he avoided prosecution for the gruesome bludgeoning of an Oklahoma man by agreeing to testify for the state. The next year, he received a five-year deferred sentence after pleading guilty to an attack on a woman outside a Washington state shopping mall. In 1976 he admitted raping another Arkansas woman, but was not prosecuted when the woman refused to testify.

In 1984, in Forrest City, a small town in the Delta named after the Ku Klux Klan's founder, Mr DuMond raped a teenage cheerleader who was a distant cousin of Bill Clinton. While awaiting trial, he was bound and castrated with a razor blade and fishing wire in his own home by vigilantes who were never identified. A few weeks later, fire destroyed his house. For a time, the county sheriff kept Mr DuMond's testicles in a jar in his office and invited the media to view them. Although some people doubted the rape, Mr DuMond was sentenced to life in prison in 1985.

Mr DuMond became a legend in Arkansas politics. Mr Clinton's many enemies claimed that he had been framed by politicians trying to gain favour both with Mr Clinton and with another local grandee. In the early 1990s, Mr Clinton, away on the campaign trail, passed on Mr DuMond's requests for parole to his lieutenant-governor, Jim Guy Tucker. Mr Tucker, who was elevated to governor when Mr Clinton went to the White House, duly commuted Mr DuMond's sentence from life to 39 years and six months.

But Mr Tucker, who got entangled in the Whitewater mess, was ousted from office in 1996. The DuMond case then passed to his Republican successor, Mike Huckabee, who announced his intention to free the prisoner. Democrats dismissed this as Clinton-bashing. But in 1997 Mr Huckabee started the process of granting clemency, until a public outcry caused him to draw back. In his letter to Mr DuMond denying clemency, he nevertheless wrote: "My desire is that you be released from prison."

By coincidence, on that same day, the Arkansas Post Prison Transfer Board voted to parole Mr DuMond on condition that he leave Arkansas. Board members now say that Mr Huckabee put pressure on them to release him; the governor denies it. But both Texas and Florida refused to take Mr DuMond, so he stayed in prison. In 1999, having served 14 years (about four more than the average convicted rapist in Arkansas), Mr DuMond was released by the parole board to live with a relative in southern Arkansas. Last year, he got married and moved to Missouri, where he now faces the new murder charge.

While Mr DuMond stews in a Missouri jail, Democrats in Arkansas claim that Mr DuMond will be Mr Huckabee's "Willie Horton" during next year's gubernatorial campaign (Mr Horton, a Massachusetts prisoner who was let out on a weekend pass and committed a murder, was used to much effect by Republicans against the state's then governor, Michael Dukakis, during the latter's 1988 presidential campaign). Mr Huckabee plays this down, pointing out that it was Messrs Clinton and Tucker who started

the ball rolling. His approval rating is also still above 75%.

But Arkansas politics can be as volatile as it is dirty, and the governor's professed keenness to let Mr DuMond go free may make him vulnerable. Even some of his supporters think an apology might be in order. That, though, would mean a victory of sorts for Mr Clinton: something no Arkansas Republican could countenance.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Missile tests

If at first you don't succeed...

Jul 19th 2001
From The Economist print edition

A timely hit in space has helped the Pentagon's case

Shooting star?

THIS time, nobody could accuse the Pentagon of building up unrealistic expectations. In the run-up to its fourth attempt to stop a long-range ballistic missile as it hurtled through space on July 14th, the Defence Department insisted again and again that it did not really matter much whether the $100m experiment worked.

What were test failures, anyway—so the argument went—except a healthy sign that new ideas were being tried out, and new conclusions being drawn? As Paul Wolfowitz, the deputy defence secretary, told Congress, all the best arms programmes began with one setback after another. "Failure is how we learn," he insisted. "If a programme never suffers test failures, it means someone is not taking enough risks or pushing the envelope."

In fact, the test went according to plan—or so the Pentagon, very cautiously, asserts. First an intercontinental ballistic missile, carrying a mock warhead, was launched from an air base north of Los Angeles. Simultaneously, a decoy balloon was fired in a similar direction. Then, about 20 minutes later and 5,000 miles away, an interceptor rocket carrying a small "kill vehicle" was unleashed from the Kwajalein atoll in the Marshall Islands; within eight minutes, the killer had detached itself, figured out which was the fake target and collided with the real one at more than 16,000 miles per hour.

Pictures relayed to the Pentagon showed an impressive flash of light; there was cheering in the control room. True to his low-key style, Donald Rumsfeld, the defence secretary, followed proceedings from home for the reason—his spokeswoman said—that it was "just a test".

Should American taxpayers be concerned, then, that not enough risks are being taken or envelopes pushed? In one sense, yes. The target was cone-shaped, whereas the decoy was round, and there was only one of them. In real life, there might be lots of decoys, and they would be identical in shape to the real target.

But politically, of course, it was a pleasure to hit the target, particularly at a time when doubts about the whole idea of sharply increased spending on missile defences are growing among Democrats. The two tests last year were both embarrassing failures. The first one, in October 1999, appeared to be successful but was later pronounced a partial failure after it turned out that the interceptor at first homed in on the decoy, not the real target. This time the Pentagon is stressing that it will take several weeks to analyse the data from the test and see whether everything really worked.

In any case, the promotion of a "culture of failure" has a purpose which goes far beyond this month's experiment. Mr Rumsfeld has given notice of a sharp acceleration in the pace of testing, designed to create, as quickly as possible, an anti-missile defence system consisting of three "layers"—in other words, with the ability to hit missiles during their ascent, at their mid-point, and on their way down. In 2002 alone there will be ten tests, and the number could rise if there are any setbacks. Experimental interceptor silos will be built at two sites in Alaska.

Philip Coyle, who supervised the Pentagon's testing programme until a few months ago, but has since joined a left-wing lobby group, the Centre for Defence Information, believes that his erstwhile masters should at least be given credit for consistency. "If they are serious about acquiring layered anti-missile defences as soon as possible, they are doing the right thing," he says. By his calculation, each layer will

take up to 24 “developmental” tests (in other words, tests in which the conditions are rigged to be more benign); only then can operational tests, designed to reproduce real-life conditions, begin.

Assuming at least ten tests a year, it might be realistic to deploy a reliable defence against a limited strike by about 2010, Mr Coyle reckons. The Pentagon has suggested that a provisional shield might be erected much sooner, using equipment which had not yet been fully tested. But Mr Coyle predicts that the Pentagon’s regional commanders-in-chief will be reluctant to take into service assets whose reliability is still in question.

Another point on which Mr Coyle differs from his former bosses is their contention that pursuit of an anti-missile defence system will inevitably “bump up against” the Anti-Ballistic Missile treaty within a matter of months. In his view, the ground-based solution being tested this month can be pursued for several more years without breaking the treaty. As for the sea-based or air-based defences that Mr Rumsfeld also wants to develop, they would violate the treaty (which permits only a limited number of fixed, land-based interceptors) once they were deployed. But the Pentagon does not yet have the ability to test treaty-busting interceptors launched from the sea or the air.

In the longer run, though, sea-based systems, designed to strike missiles during their ascent, have big attractions. And if the Pentagon is sincere in saying that its main concern is with unpredictable little dictatorships (all the current examples of which happen to have coastlines), it may be possible to win Russian assent to the deployment of interceptors at sea. It has not been a bad week for Mr Rumsfeld.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

California's power crisis

How to keep the fans turning

Jul 19th 2001 | LOS ANGELES, SACRAMENTO AND SAN FRANCISCO
From The Economist print edition

As it wrestles with its convoluted electricity crisis, California is slowly teaching America how—and how not—to manage power

"ELECTRICITY is too essential to be left to the market...It is a critical, life-giving resource, not a commodity." So says Medea Benjamin of Global Exchange, a San Francisco-based group best known for opposing globalisation. Now it is turning its fury on electricity deregulation. Ms Benjamin, a Green Party Senate candidate last year, is leading a grass-roots movement to put the whole country's electricity industry under municipal control. With ballot initiatives in San Francisco, San Diego and other cities, the "public power" movement is the one clear winner from this year's power cuts and price rises.

A bright future for the governor?

The idea that California, home of Reaganomics and Silicon Valley, should now embrace socialism is not as far-fetched as it sounds. Anti-market forces have been fuelled by a botched deregulation five years ago of the state's power sector that has led to soaring prices, near-bankrupt utilities, and black-outs.

In a striking display of "public power", the state government has stepped in to buy wholesale power on behalf of its utilities. Now it is trying to buy the power grid. Gray Davis, California's governor, has even created a state Power Authority and anointed David Freeman, a wily veteran of government-run power agencies, as his "energy tsar".

Faced with this astonishing expansion of public power, some in the California legislature have been trying to rein in Mr Davis's ambitions. Legislators this week debated whether to approve his plan to keep Southern California Edison (SCE), a big utility, from bankruptcy by buying its grid assets for the inflated price of $2.76 billion. Separately, the governor is also buying the grid assets of another utility, San Diego Gas & Electric (SDG&E), which remains healthy. One assemblyman from his own party put it this way: "If we've demonstrated anything in the past few months, it's that the state of California has no business being in the power business."

Yet the state looks likely to remain in the power business for years, especially if things get worse. The Independent System Operator (ISO), which runs the grid, has forecast some 260 hours of black-outs this year. Economists at the University of California at Los Angeles worry that the power crunch will drag the state's economy, the world's fifth biggest, into recession. Even the energy tsar is cautious: "We've just landed at Normandy, but it's a long way to Berlin—and we may yet have to fight a Battle of the Bulge."

The state has a bad record to live down. Mr Davis's early handling of the power crisis was disastrous. He ignored the first warning signs, which came a year ago with price spikes in San Diego, and struggled for months to work out what to do. By reacting so slowly, Mr Davis may have cost taxpayers some $20 billion. This year, the state expects power costs to top $50 billion, up from $7 billion in 1999.

Still, the governor can no longer be accused of doing nothing. On the supply side, he has just helped hustle into service three power plants, the first big plants to open in the state in a decade. The demand picture is better, too: thanks to conservation, demand is a tenth or so below last year's level. More encouragingly, the peak price of power on the wholesale market has dropped considerably since March. Mr Davis, naturally, claims credit for that.

The Californian answer

His longer-term plan has three parts. First, the state is pushing public power, as is seen in the new power authority and in Mr Davis's attempts to buy the grid. Second, it is purchasing long-term contracts: Mr Freeman negotiated a clutch of these a few months ago, at the height of the crisis. Third, it is pummelling producers ("price-gougers" and "bloodsuckers", as Mr Davis prefers to call them) through price caps and rebates. After months of resisting his calls, the Federal Energy Regulatory Commission (FERC), America's top electricity regulator, agreed in June to impose "soft" caps on wholesale prices. The FERC is also considering Mr Davis's claim that generating firms should pay a $9 billion refund.

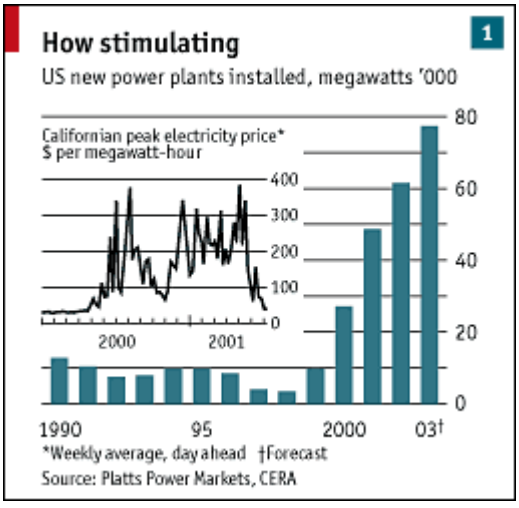
Do these three things add up to a coherent policy? Take **public power** first. Even market-minded experts accept that some state intervention was necessary to resolve the crisis, but most of them argue that the state should withdraw once the botched deregulation is set right.

It may not. The governor has sweeping powers to build and seize plants, and he has, in effect, taken over the state's ISO. The newly created power authority answers to him directly, not to regulators, and the new energy tsar insists that the authority is not temporary. He also promises to seize plants only as "a last resort", but may find it hard to restrain himself: in early July, a committee of the state Senate passed a resolution encouraging him to "commandeer" plants. Loretta Lynch, the head of the Public Utilities Commission, the state's top regulatory body, wants deregulation to be scrapped altogether and the state to return to "cost-based pricing" regulation.

Since Mr Davis long opposed efforts to increase retail rates to pass on those higher wholesale costs, the bill for power will be mostly picked up by taxpayers. To keep the state's coffers full, it has tried to use its good (though fading) credit rating to tap the financial markets. Mr Davis plans to float a $13 billion bond (the largest-ever municipal offering in America) later this year.

What about long-term **power-purchasing agreements**? The governor's men insist that the recent drop in wholesale prices owes much to the long-term contracts. One reason to think otherwise is the astonishing number of power plants now being built across America (see chart 1). This supply-side surge is a natural response to the sky-high wholesale prices of the past year—and one that would have produced lower prices anyway, long-term contracts or not. On current trends, there will be a glut in two years' time. Joe Zenker of Cambridge Energy Research Associates, a consultancy, reckons the contracts may even have propped prices up.

Another critic is Kathleen Connell, the state's controller. "I dispute the governor's assertion that long-term contracts have reduced prices," she says. "We are now committed to long-term high prices negotiated in a short-term panic." The governor's aides say that the average price of electricity reflected in those contracts, which make up the lion's share of the state's needs over the next decade and beyond, is about seven cents per kw-hour. No doubt that seemed a bargain back in March, when prices had soared past 15 cents per kw-hour, but it already looks excessive today—never mind when the glut arrives.

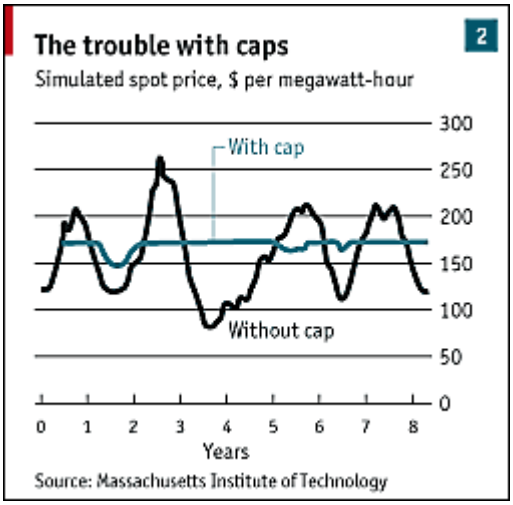


And **price caps**? The governor insists the FERC's decision, on June 19th, to impose a limit on what generators can charge California and other western states prompted the recent price decline. It is possible that these price caps have splashed cold water on an overheated wholesale market. But prices were heading down anyway thanks to increased supply. The great danger, as this paper has argued, is that the caps will not remain temporary: and that, if they stay, they will discourage fresh supply.

A good new study from the Massachusetts Institute of Technology illustrates the pitfalls. It shows that price caps can moderate price spikes, but at an unacceptable cost: capping prices dampens price signals and discourages investment, so shortages result. The perverse result is that the capped price can be higher than the level achieved without caps (see chart 2)—and that the average long-term capped price may be higher than the uncapped price.

For all this, there may be a silver lining in the cloud. Spurred by

California's mess, federal officials are looking more widely at failures in the wholesale power market. One area where Mr Davis can claim a political victory, if not necessarily a financial one, concerns the **abuse of market power** by generators. For months now, he has argued that this is the root cause of his state's power crisis. He has asked the FERC to investigate suspicious breakdowns at power plants, possible collusion and other things that, he claims, have jacked up prices.



The FERC, led by its market-minded boss, Curtis Hébert, has generally been sceptical. But about a month ago the FERC's commissioners appointed a judge to supervise negotiations between the state and its power suppliers over refunds claimed by the state for alleged price gouging. Although the judge rejected California's demand for $9 billion, he agreed that its allegation of price gouging was justified. As those talks broke down, the FERC's commissioners must decide the case.

An explosive new report by the General Accounting Office, a federal watchdog agency, also suggests that the FERC has been negligent. The agency will now work to develop a new test of market power that may not allow suppliers to earn market rates in regional markets (like California) that it decides are "dysfunctional"—in other words, non-competitive. A reflective Mr Hébert says his agency has learned from this crisis: "Looking in the rear-view mirror, we should have jumped in quicker with California."

The next weak link in the power-deregulation chain is **transmission and distribution**. Officials in California reformed the wholesale and retail power markets, but neglected the grid. As wholesale trading has expanded, bottlenecks have built up in various places. One example is Path 15, the chief grid connection linking the northern half of the state with the southern half. Black-outs have sometimes occurred simply because power has been choked off.

Mr Davis has come up with a blunt answer: he wants the state to control the grid. Stephen Baum, the boss of Sempra Energy (which controls SDG&E), thinks this is a sound plan. But the better way would be for regulators to consolidate America's balkanised grid into just a few independent, regional operators, and then to give them strong incentives to upgrade the system. In this, too, California seems to have had a positive effect. On July 11th, the FERC boldly ordered just such a consolidation.

An even better way to get round bottlenecks is to expand distributed generation, or **micropower**. By placing small units close to the end-user, utilities (or end-users) need not in the first place send so much power down those ageing lines.

In the past, utilities sometimes used high "standby" charges or bogus safety worries to obstruct micropower. No longer, insists the energy tsar. The state recently decreed that all "standby" charges are to be waived for the next two years for micropower units. "The utilities in the state are no longer capable of resisting," Mr Freeman insists. "They are broke! And the people simply lack confidence in the grid's reliability."

Thanks to those pricey long-term contracts, the economics of micropower look better than ever. Micropower technologies, ranging from fuel cells to microturbines to small natural-gas plants, are taking off. Mark Bernstein of the Rand Corporation, a think-tank, says firms are now taking even solar power seriously.

Getting the signal

Another flaw in California's deregulation was the fact that retail tariffs were fixed even as wholesale prices were freed. Having received no **retail price signals**, consumers had no incentive to reduce consumption, no matter how high the wholesale price. Regulators have recently raised rates, but the new rates are fixed, too: they do not fluctuate with load, and so do not send price signals. Only introducing real-time meters and real-time pricing for all customers would do that.

Proper pricing is some years off, but regulators are at last dipping their toes into the water by installing smart meters as part of a trial. Estimates by the Electric Power Research Institute suggest that a drop in Californian demand of only 2.5% during a power crunch could reduce the wholesale peak price by up to

24%.

The best news of all is that California's power crisis may finally have provided a wake-up call to Americans, the world's biggest guzzlers of energy. There are already moves afoot, for example, to improve the efficiency of public-lighting fixtures and to reduce the vast quantities of power wasted by appliances in "stand-by" mode. More generally, California's troubles have strengthened the case for valuing power properly and using it efficiently. A genuinely competitive market—with a vigilant regulator and proper price signals—is surely a better way to achieve that than adding further layers of bureaucracy. By trial and by error, California continues to light the way for the rest of America.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Lexington

The incredible shrinking VP

Jul 19th 2001
From The Economist print edition

Something is happening to Dick Cheney

DICK CHENEY spent part of this week doing one of the most dismal jobs in the world: holding town-hall meetings to try to sell his energy policy to a sceptical America. He was suffering from such a bad case of laryngitis that he had to sit by impassively while his wife delivered his speeches for him. And his speeches included the sort of touchy-feely tosh—"conservation is a must"—that Mr Cheney despises.

Most vice-presidents start off with no influence and then gradually try to acquire some. Mr Cheney may be doing the reverse. A few months ago, praise was heaped on him. This column, it should be admitted, was the first to compare him to a prime minister. Others depicted him as a father-figure, a Mr Fixit, a steady hand and a Grand Panjandrum. He ran the transition, chaired cabinet meetings, co-ordinated relations with Capitol Hill. All roads in Washington led to Mr Cheney.

But now he is a much diminished figure. The former oil man is the prime exhibit for the argument that the Bush administration is more interested in producers than consumers. He is being required to do more of the mundane jobs that traditionally burden vice-presidents: attending boring functions, tapping fat cats for further contributions, and floating trial balloons. Rather than beating a path to his door, Washington is whispering about how far the shrinking will go. Might Mr Cheney even be dropped from the ticket in 2004?

The most obvious reason for this detumescence is that his early prominence was too good to last. Mr Cheney inevitably attracted a huge amount of attention as a comparative Washington insider in a predominantly Texan entourage. He helped to dispel fears that the young Texan rube would be out of his depth in Washington. He was also the natural choice to run the transition, having been involved in three of them in the past.

But George Bush and his team are no longer strangers to Washington. Mr Bush has earned his spurs by pushing the tax cut through Congress. People like his national security adviser, Condoleezza Rice, are visibly more confident in their jobs. Karl Rove, his senior adviser, regards himself as the grand master of political strategy. Mr Cheney is just one voice among many. His reputation suffers, too, from one of his greatest virtues: that he is so self-effacing. Most vice-presidents, no matter how loyal, cherish dreams of following their bosses to the Oval Office. But Mr Cheney has no ambition to become president.

There is also a more malicious explanation for Mr Cheney's diminishing profile. The vice-president's fingerprints are on both of the administration's biggest muck-ups. He was responsible for fashioning its energy policy, which has become Mr Bush's equivalent of Bill Clinton's "gays in the armed forces" fiasco. It was Mr Cheney who growled that conservation was nothing more than "personal virtue", and now there is a fuss about the vice-president off-loading the energy costs of his residence—$186,000 and rising—on to the navy's budget. Even worse, maybe, as the man responsible for managing the administration's relations with Congress, Mr Cheney stands accused of having lost Jim Jeffords, the Vermont senator who decided to abandon the Republicans because the White House had supposedly paid too little attention to him.

Rockefeller's revenge

To blame Mr Cheney for these troubles is not entirely fair. Mr Bush's own connections with the oil industry always made him vulnerable on energy. Mr Jeffords was probably going to quit anyway—and his beef seems to have been with Mr Bush rather than Mr Cheney. The vice-president is plainly the target of a fair amount of back-stabbing. But that in itself is a sign of another problem. All White Houses are ultimately organised to boost the president's reputation over everybody else's. The Texan mafia that surrounds Mr Bush is particularly protective of its boss. It bristled at all the jokes on "Saturday Night Live" about Mr Cheney being the real president. It is now working hard to demonstrate that Mr Bush is really the man in charge.

And it has the perfect excuse to do so: Mr Cheney's health. The fact that he has had three heart procedures since becoming vice-president is an argument for giving him a rather lighter workload. It is also an argument for making sure that he is less than indispensable to the administration. A few months ago Mr Cheney's death might have destabilised the young administration. Now Mr Bush can survive without his former mentor.

Mr Cheney can take comfort from the fact that he is still the most powerful vice-president in recent history. At this stage in his spell in office, Al Gore was still hidden from view, grinding away at his "reinventing-government" job, where he had been parked by the Clintonites. But Paul Light of the Brookings Institution points out that Mr Cheney may have further to fall.

The Bush loyalists know the president will face a tough fight in 2004, and are well aware of the electoral arithmetic. Mr Cheney is an uninspiring campaigner. He comes from Wyoming, a reliably Republican state that has only three electoral votes. And the quality that most recommended him to the Bush ticket—his insider's knowledge of Washington—is a fading asset as Mr Bush gains experience. Tom Ridge, who could help to deliver Pennsylvania's 23 votes, and Colin Powell, who could galvanise moderate voters, are often mentioned as replacements.

Mr Light speculates that Mr Cheney may be much more like Nelson Rockefeller than Mr Gore. Rockefeller started off as an indispensable prop to Gerald Ford. He was a considerable power-broker in the party and untainted by ties to Mr Ford's conspiratorial predecessor, Richard Nixon. But over the next four years his position was progressively undermined as he was first stripped of important positions and then dropped from the 1976 ticket. One of the masterminds behind this policy of vice-presidential destruction was a rising young chief of staff: Dick Cheney.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Argentina's economic crisis

Austerity, or bust

Jul 19th 2001 | BUENOS AIRES
From The Economist print edition

A drastic austerity plan will test the government's shaky political support

Get article background

EPA

WHEN Domingo Cavallo was Argentina's economy minister in the early 1990s, his arrival at Buenos Aires restaurants was sometimes greeted with applause from diners grateful to him for killing inflation and delivering growth by fixing the peso at par to the dollar. Four months ago, when President Fernando de la Rua turned to Mr Cavallo to try to haul the country out of a recession that has now lasted three years, Argentines again expected miracles. But on July 14th, when Mr Cavallo escorted his daughter to her sumptuous wedding, they were pelted with eggs by angry demonstrators.

That summed up the surly mood with which Argentina greeted Mr Cavallo's last-ditch effort to stave off a debt default and devaluation. This involves emergency cuts in government spending, aimed at immediately eliminating the fiscal deficit. "We will spend only what we collect in revenues and we will fight [tax] evasion to eliminate the deficit and our dependence on expensive loans," said a tired-looking Mr Cavallo, after admitting that Argentina "had no more credit".

At first, the public reacted by queuing up to take their money out of the banks, prompting shortages of dollars. Bankers reported a brisk demand for safe-deposit boxes; Argentines have seen enough economic crises to know that dollar accounts can be forcibly converted to devalued pesos by governments.

But the seriousness of Argentina's plight prompted the country's warring politicians to rally round last weekend. With uncharacteristic determination, Mr de la Rua led the effort to get political backing for the "zero-deficit" plan, insisting that it was "non-negotiable". He won grudging support from his own Radical Party, including Raul Alfonsin, a former president who has frequently sniped at austerity plans. On July 16th leaders of the Peronist opposition followed suit, promising to balance the budget in the provinces they govern. Businesses, too, have been prompted to sudden generosity: banks, pension-fund administrators and privatised utilities promised to advance up to $1 billion against next year's tax payments.

The risk of non-stick measures

To avoid a repeat of last week's debacle in which it struggled to sell treasury bills, the government was reported to be pressing pension funds to exchange short-term government bonds for longer-term paper at a "patriotic" interest rate. But after a couple of calmer days in the financial markets, doubts surfaced again. The first question was whether the measures would stick. Mr Cavallo wants to trim total government spending by $1.5 billion this year and $4.3 billion next. The country's provincial governors have been given the freedom to choose how they balance their budgets. Mr Cavallo will cut central-government salaries and pensions by 13% for the next three months; they would be increased again only if tax revenues allowed.

These cuts face fierce opposition: trade unions staged strikes this week. Many in Mr de la Rua's Alliance, including Mr Alfonsin, argue that the budget gap should be closed by increasing taxes, such as those on privatised utilities and pension funds. Indeed, Carlos Ruckauf, the Peronist governor of Buenos Aires

province, claimed that he faced a “default situation” after Alliance members in the provincial legislature blocked cuts. Mr Cavallo’s decrees cutting wages will be challenged in Congress and the courts—though officials were confident of victory.

The second difficulty is that, in the short term, the cuts will prolong Argentina’s three-year recession. The current effort is the seventh austerity plan since Mr de la Rua came to office in December 1999. The previous ones were either diluted away by political opposition, or their effect was neutered by lower tax revenues, as economic activity fell. That is why, on taking office, Mr Cavallo scorned such measures in favour of tinkering with tariffs and taxes to try to stimulate growth. But the government’s desperate hope is that if it pulls out of the local credit market, interest rates will fall, allowing growth to resume by the end of the year.

That is still a long way off. Political support for the government remains shaky: Mr de la Rua is deeply unpopular, and a congressional election is due in October. Mr Cavallo’s stock is falling, too. He is notoriously irascible; he was kept away from crucial talks with the Peronists after picking a gratuitous row with Mr Ruckauf. Some of Mr de la Rua’s advisers urge him to form a new cross-party coalition, based on Mr Cavallo’s small party and the Peronist governors, who are more appreciative of economic orthodoxy than many of Mr de la Rua’s nominal supporters.

Argentina has two underlying problems. One is the rigidity of its exchange-rate peg, and the strength of the dollar. About this, the government can do little except wait for the dollar to weaken; in a largely dollarised economy, a devaluation would cause carnage. The other problem is a state bloated by pork-barrel spending and hampered by a creaky tax system. Rather than tackle this, for ten years governments borrowed. Now time has run out. The choices are austerity or bust.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Tourism in Peru

Road to ruin

Jul 19th 2001 | CUSCO
From The Economist print edition

Popularity brings its own problems

THE day after being sworn in as Peru's new president in Lima, the capital, on July 28th, Alejandro Toledo plans to repeat the ceremony among the mighty terraces and temples of the Inca citadel of Machu Picchu. For Mr Toledo that is a way of celebrating his achievement in becoming Peru's first elected president of indigenous descent. He also says it will boost the country's $1 billion-a-year tourism industry, which he sees as a good bet for much-needed jobs. But can the fragile ruins of Machu Picchu stand so much attention?

Sheltered by clouds on an Andean ridge in the high rainforest of Cusco, Machu Picchu was "discovered" only in 1911. Now it is Peru's most famous attraction, and is increasingly besieged. In an accident during the making of a beer commercial last year, a cameraman crashed on to a sacred sundial called the *Intihuatana*, snapping off a small section of the stone. Then a Japanese scientist caused further alarm: he claimed that Machu Picchu was slipping downhill, only to say later that he had been misquoted when officials affirmed that the citadel was resting solidly on a granite block.

But the biggest long-term threat is Machu Picchu's fast-growing popularity with tourists. Each year some 300,000 visit the site, which is surrounded by a large nature reserve sheltering more than 400 species of birds and dozens of rare orchids. In the dry season (May to September), up to 2,200 people tramp around the ruins each day. With them come problems: the gradual erosion of the Inca roads to the site; the chaotic growth of Aguas Calientes, a nearby village that has become an ugly town; and rubbish and other pollution at the ruins.

Part of the problem is poor management. Jurisdiction over Machu Picchu is shared by a gaggle of local and national authorities. In 1996 a five-year plan was drawn up to streamline the running of the site and its environment, financed by a $6.1m debt-swap agreement with Finland. There has been some progress. The nature reserve now has its own management unit. There are plans to seal an open-air rubbish tip at Aguas Calientes, and to spruce up the town. But only half of the money has been spent, partly because Finland insists that environmental projects should be undertaken only if the local authorities agree to keep them going by using part of the revenues from ticket sales for entry to the site.

With Machu Picchu close to capacity, if the tourist industry is to grow, as Mr Toledo hopes, Peru needs to boost the appeal of the country's wealth of less famous cultural and natural wonders. Last year, though around 70% of the 1m tourists who went to Peru visited Cusco, less than 40% visted the next places on the popularity ratings, Puno and Arequipa.

Tourism businesses are starting to heed the call to diversify. PeruRail, a joint- venture between Orient Express, a British luxury tourism outfit, and a local company, is investing $17m to modernise the railway between Arequipa, Puno and Machu Picchu. In April the company launched a plush service from Cusco to Puno using Pullman-style rolling stock. Tourists can make a side-trip to the Colca Canyon, where condors fly through one of the deepest gorges in the world.

Alas, such plans were dealt a temporary blow last month, when an earthquake hit southern Peru, killing more than 140 people and leaving 200,000 homeless. One of the towers of Arequipa's handsome

cathedral of white volcanic stone toppled backwards through the roof in a cloud of dust and rubble. The damage to the city's colonial centre was otherwise remarkably light. Even so, many tourists have cancelled plans to visit Arequipa.

But in a country rarely short of bad news, the underlying trend for Peru's tourist industry remains one of steady growth. Managing the growth so that the increase in jobs does not come at the expense of the sites the tourists wish to visit will be the next task for Mr Toledo—once he has communed with the Sun God.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Mexico's foreign policy

Branching out

Jul 19th 2001 | MEXICO CITY
From The Economist print edition

The country has worldwide ambitions, but its destiny is North American

VICENTE FOX, Mexico's new president, was in Chicago and Detroit this week, pushing some big ideas, such as turning his country into the world's car-making hub, and urging George Bush to legalise some 3m Mexicans living and working illegally in the United States. Pipedreams? Perhaps. But Mr Fox has quickly made his mark north of the border. Mr Bush has met his Mexican counterpart three times this year. The two men seem to like each other. At Mr Fox's urging, the two governments are looking at ways to improve the condition of Mexican migrants.

Reuters

Castañeda has views for Fox

Ambitious, outgoing, even meddling—such is Mexico's new stance abroad under Mr Fox. It is an attitude in the image of his foreign minister, Jorge Castañeda, an undiplomatic university professor. And it is a big change. For much of the seven decades of rule by the Institutional Revolutionary Party (PRI), Mexico's governments viewed the world as a place best left alone, in the hope that the world would reciprocate. Now, foreign policy has a new urgency.

Mr Castañeda was a controversial choice. Some predicted that his plain speaking would sink him, and that his left-wing background would antagonise Republicans north of the border. Rumours (which he denies) that he may form a new left-wing political force make the president's conservative National Action Party uneasy. One of Mr Castañeda's conditions for accepting the job was that Mr Fox should at least listen to his views on all other matters too, and there is said to have been friction between him and other cabinet members. But as a diplomat he has done distinctly well. The new government has been more innovative, and probably more successful, in foreign policy than in any other sphere.

The traditionally prickly relationship with the United States is more co-operative. Take migration, which Mr Fox sees as part of "deepening" the North American Free-Trade Agreement (NAFTA). He says that, if the United States legalised existing Mexican immigrants, Mexico would do more to reduce the flow of new ones, by developing poor regions but also by an unprecedented offer to police its own border zone and migrant routes. That has already prompted growls in Mexico, and claims that it violates the constitutional right to freedom of movement. Also new is Mexico's readiness to extradite drug-traffickers and other criminals wanted across the border. The United States Congress, for its part, is debating a proposal to suspend its annual practice of "certifying" countries for their co-operation in the drug war, a ritual especially resented in Mexico.

Next, Mexico wants to improve its ties with Latin America, which NAFTA caused it to neglect. It is trying to support Colombia's search for peace by putting pressure on the FARC guerrillas; it has offered to work together with Colombia in fighting drugs. Mr Fox is promoting an ambitious joint development scheme for Central America, called the Puebla-Panama Plan.

Mexico is also being more active in international bodies. It is vocal on human-rights issues that it used to be attacked for. And the government has continued the previous administration's policy of cooling its once friendly relations with Fidel Castro's Cuba.

The logic to all this activity, says Mr Castañeda, is that Mexico wants to learn from other countries, so it is getting more involved in their affairs. Foreign diplomats report that the government does listen. "There is an openness to ideas and willingness to discuss things, which is surely in Mexico's long-term interest,"

says Adrian Thorpe, the British ambassador.

Not everyone is happy, though. Members of the Asia-Pacific Economic Co-operation forum (APEC), which will hold a summit in Mexico next year, are frustrated at its lack of preparation. Despite having added trade promotion to his portfolio, Mr Castañeda has handed the summit over to the economy ministry. At a recent lunch with APEC ambassadors he raised more hackles by refusing even to discuss it. Another criticism is that he is neglecting the inner workings of his ministry. That looks like a mistake. Partly because of the PRI's approach to foreign policy, Mexico's diplomatic service lacks the professionalism of, say, Brazil's.

For all its wider muscle-flexing, Mexico cannot avoid ever-closer ties within North America. For years Mexican politicians have paid lip service to the idea of a Free-Trade Area of the Americas (FTAA), which would give the rest of Latin America better access to the markets of the United States and Canada. Mr Castañeda is more honest: the FTAA is "not a big deal" for Mexico, he says. That is because its NAFTA partners already take more than 90% of Mexico's exports, and it already has bilateral trade pacts with much of Latin America.

Mexico likes to see itself as a bridge between Latin America and the United States. But it is a bridge with barriers. Last month it announced tighter controls on its border with Guatemala. In return for closer ties with the United States, Mexico seems willing to act as a cushion against migration. To critics, that contradicts the spirit of the Puebla-Panama Plan. "How can they do that and claim they want closer ties with us at the same time?" asks a Central American diplomat. When the United States beefed up its own border defences for the onset of NAFTA in 1994, some Mexicans asked the same question. But Mexico's new foreign policy is pragmatic. The government knows very well where the country's destiny lies.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Rebuilding El Salvador

Homeless, and increasingly hopeless

Jul 19th 2001 | SANTA TECLA
From The Economist print edition

How do you rehouse a quarter of a country?

TEN thousand, four hundred and twenty-four aftershocks, and counting. El Salvadoreans still feel the reverberations of the three separate earthquakes that hit them in January and February this year. The loss of 335,000 homes either destroyed or badly damaged, which amounts to a quarter of the country's housing, will be felt for much longer.

The authorities reacted fairly fast in the immediate aftermath of the earthquakes, putting up over 200,000 temporary shelters in time for the start of the rainy season in June. But lasting solutions are harder.

The government has found sites for new settlements, either on public land or by buying private land. It is offering cheap loans to help the slightly better-off build their own homes. It is also trying to expand existing programmes, such as an "adopt-a-home" scheme for foreign donors and Salvadoreans living abroad. In the cramped offices of the housing ministry, an American prospective philanthropist peruses a list of contractors offering houses for $2,000-4,000 apiece. An official explains that he needs no permit; he just has to go to one of the new settlement sites and tell the builders where he wants the house.

The government has appealed for foreign aid to pay for homes for the poor. But so far, says Cesar Alvarado, the minister for housing, it has enough money for fewer than 30,000 homes. Of those, only 5,000 have been built, though a legion of non-governmental organisations are putting up another 5,000. The official target is to build 100,000 low-income homes within two years. Unless the government seeks more allies, that looks unreachable.

Worse, the target underestimates the need. Officials say that some 50,000 families live in high-risk zones. One of these is Las Colinas, a housing development in the town of Santa Tecla, where more than 1,000 people died in January when a single, devastating landslide came down on them. At Las Colinas, people are already moving back into houses on either side of the empty swathe cut by the landslide.

Whether such families eventually leave their homes is up to them. Few are likely to do so. Even before the quakes, according to official figures, there were 40,000 homeless families and over half a million people living in houses without a proper roof, floor or walls. Although almost 50,000 new homes were being built each year, they were barely enough to keep up with the deficit. To force people out of areas they have lived in for years would make the shortage worse, as well as being politically risky.

Those who have moved face new problems. Some 800 families from Santa Tecla, for instance, are now living on what was to be the site of a prison 25km (15 miles) from their old homes. Even if they could get to where they used to work, says Mario Ernesto Melendez, a community leader, they might find they had no jobs: the earthquake put paid to many businesses. Some people are finding work building houses. But a lot more housebuilding is needed, and fast.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

India and Pakistan

Summit ascended, but Kashmir not yet broached

Jul 19th 2001 | AGRA
From The Economist print edition

The Indo-Pakistani summit came close to success, and may yet achieve it if the hardliners on both sides can be restrained

AP

JUST before midnight on July 16th, President Pervez Musharraf, Pakistan's military ruler, put a dramatic end to a three-day summit in the Indian city of Agra by walking out of a final meeting with India's prime minister, Atal Behari Vajpayee, and flying home to Islamabad. The summit had begun two days earlier with expansive gestures and well-choreographed symbolism. But it appeared to have broken down so badly over the disputed state of Kashmir and cross-border terrorism that there were immediate fears that the two nuclear powers would be tempted to step up their border skirmishes.

Yet, a day later, both sides were insisting that there had been no breakdown, just a disagreement over a few words in a proposed declaration, which could be solved when they next met. First, the two foreign ministers held press conferences that mixed recriminations with hopes for the future. More significantly, both Mr Vajpayee and General Musharraf then addressed their top officials and seemed to be trying to sideline their critics and sustain the momentum for talks. Mr Vajpayee even told his Council of Ministers that the summit had been "successful".

It is not yet clear whether this will turn out to be merely an exercise in damage limitation or evidence of a meeting of minds between two leaders who may now be able to pull their countries closer together. Certainly, these two very different men—one a slow-speaking 74-year-old veteran politician, the other a loquacious but tough 57-year-old general who made himself president last month—seem to have got on unexpectedly well together. They met alone for almost six hours during the summit and it looks as though the eventual failure to reach agreement was caused more by their hardline ministers and advisers than by their own unwillingness to come to terms.

General Musharraf had set an unexpectedly favourable tone when he arrived in India on July 14th. At the tomb of Mahatma Gandhi, the father of the Indian nation, he praised Mr Gandhi's "struggle for non-violence and peace". In the evening he surprised his hosts by admitting at a banquet that there could be "no military solution" to the 54-year-old dispute over Kashmir—a significant statement for the chief of army staff who had directed Pakistan's unsuccessful battles with India at Kargil in Kashmir two years ago. He added that the summit should set out to solve the issue "once and for all".

A joint declaration that was readied for signature on Monday provided for annual summits between the two leaders and six-monthly meetings between their foreign ministers. It listed nine points for discussion, including the Siachen Glacier, where the two countries have waged an expensive and inconclusive battle for 17 years, other disputed border issues, narcotics, nuclear safeguards and trade.

But Kashmir dogged progress. On the second day of talking Sushma Swaraj, India's information minister, pointedly failed to include Kashmir among the topics that she told journalists had been discussed. Pakistan responded with a terse statement

stressing Kashmir's centrality to any talks, and General Musharraf next morning went on television for over an hour, repeatedly telling Indian editors over breakfast that "Kashmir is the main issue". India, annoyed by such a publicity stunt in the middle of a summit, issued the text of a statement made a day earlier by Mr Vajpayee at the leaders' first meeting, when he had virtually accused Pakistan of sponsoring cross-border terrorism and said this must be included in any talks.

Some compromises were made. Pakistan had wanted India formally to accept that there was a "dispute" over Kashmir. India has consistently resisted this because it has regarded Kashmir as part of India since the two countries were partitioned in 1947 and because it does not want to open the way for possible third-party mediation. General Musharraf compromised by accepting the word "issue" instead of "dispute", but disagreement continued over how to express what both sides called the "centrality" of Kashmir.

This would probably have been ironed out had there not been a final breakdown over an associated matter—the insertion of the words "cross-border" in the declaration. It appears that the two leaders agreed that the declaration should just refer to "terrorism", but that hawks on the Indian side, apparently led by L.K. Advani, the home minister, insisted on adding "cross-border" in order to nail down Pakistan's responsibility for allowing Islamic militants to cross into India from its territory. This was a deal-breaker for the general.

The two leaders will probably meet next during the UN General Assembly in New York in September. Mr Vajpayee has also accepted an invitation to visit Pakistan but he may well hang back until there is less risk of hardliners again blocking progress because of the Kashmir and terrorism issues. This means finding a compromise that takes account of the "centrality" of the Kashmir question that is required by Pakistan, and of the "cross-border terrorism" issue demanded by India. Difficult—but certainly not impossible.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Russia and China

Remaking history

Jul 19th 2001
From The Economist print edition

Though officially friends again, Russia and China still worry about each other, not just about America

WHEN Mao Zedong, fresh from his triumph in China's civil war, signed his 1950 treaty of alliance with Stalin's Soviet Union and declared the two Communist giants' "eternal and indestructible" friendship, the free world was rightly rattled. Yet the ideological cracks soon widened to a schism. This week, as China's president, Jiang Zemin, beaming after winning the 2008 Olympics for Beijing, arrived in Moscow to sign a 20-year friendship treaty with Vladimir Putin's Russia, the superlatives had a familiar ring. But can the paper signed hide the cracks beneath it?

Their "strategic partnership" is decidedly not a military alliance but is nonetheless the foundation for a new international order, in which Russia and China are to be forever friends, never foes, enthused Mr Jiang and Mr Putin. The rhetoric was partly intended to give Mr Putin a lift ahead of this weekend's G8 summit in Genoa, where a weak Russia sits at the table with the world's richest democracies. Indeed, the new treaty is clearly meant to be one in the eye for the real power in the post-cold-war world, America. Yet there is both more, and less, to the renewed vows of Russian-Chinese friendship than an anti-American huddle.

Rhetoric aside, the new treaty may yet prove more durable than the old one by pushing the two sides to find practical solutions to some bilateral problems. As close neighbours with a troubled history, they have come a long way since their border blows of the 1960s. This week they committed themselves to settling the minor disputes that remain along their now 4,000km (2,500-mile) border. Less happily for restive Islamic and Turkic groups either side of it, they each agreed to crack down on organisations that challenge the territorial integrity of the other.

Meanwhile, trade is picking up a bit: likely to be worth about $10 billion this year, up from $8 billion last year—though this is still only a tiny fraction of China's trade with America or Japan. Unofficial cross-border trade flourishes, but many Russians worry that, without proper controls, their sparsely populated far-eastern regions could be swamped by immigrants from much more densely populated China. This week the two countries gave more substance to economic ties by agreeing to build a 2,400km pipeline to carry oil from Siberia to China's north-east.

More troublingly, for some Russians as well as for outsiders, they also intend to continue their military trade. This earns Russia about $1 billion a year from the sale to China of modern fighter aircraft, missiles, submarines and surface ships. Russia's generals worry that one day they may face a less friendly China with more Russian weapons than they have in their own armoury. Outsiders are concerned that Russia has recently agreed to sell modern conventional weapons of various sorts to North Korea and Iran too. But the sales to China cause most alarm, since they give it the weapons it needs to step up military pressure on Taiwan or press its claim to the South China Sea.

Tightening weapons ties, mutual support over Russia's war in Chechnya and China's claim to Taiwan, joint opposition to further NATO enlargement in Europe and to a closer America-Japan alliance in Asia, and a chorus of opposition to America's plans for missile defences: the list might well suggest a new anti-American alliance in the making. But the cracks are already apparent. Unlike China, which worries that America may use them to defend Taiwan against Chinese missiles, Mr Putin supports building regional anti-missile defences and is now ready to explore a new set of strategic understandings with America. The new treaty—China's initiative—is as much an effort to pin down Russia as it is a nose-thumbing gesture at America. Meanwhile, Russia is acutely conscious that its post-imperial decline coincides with the rise of China as a rival for influence and likewise wants to constrain it. The new friendship has an edge to it.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD ASIA

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

China's pollution

Exposing a dirty secret

Jul 19th 2001 | TANGAN, ANHUI PROVINCE
From The Economist print edition

Despite claims by Chinese environmental officials, rapid industrialisation is turning water supplies into black toxic soup

THE Communist Party secretary of the village of Tangan, Zhao Hezeng, surveys the yellowing stalks in the paddy fields and the tar-black water in the gully alongside. The stream that feeds the gully is brown and foamy. It too would be black were it not for a recent fall of rain. Waste from factories upstream has turned the water the village depends upon for irrigation into a foul-smelling toxic soup. Farmers get itchy rashes on their arms from working in the fields. No one dares drink from wells closest to the stream.

"The villagers are very angry," says Mr Zhao. "They want the government to sort this out, but they are not optimistic." More rain might help Tangan, in the central province of Anhui, to recover some of the rice crop in time for the September harvest. But Anhui, like much of central and northern China, is in the grip of its worst drought in years. Mr Zhao says it is possible that there will be no crop at all this year and that by winter some rice supplies may run out. Over the past 14 years, Mr Zhao has alerted the authorities several times to his village's plight, with no obvious result.

China says that environmental protection is a top priority. But it does not allow ordinary citizens to take matters into their own hands. Only a handful of tiny NGOs are allowed to work on environmental issues, and they are kept on a tight rein. Every Chinese knows that organised challenges can lead to serious trouble.

Across the country, rapid industrialisation is fouling water supplies at an alarming rate. Late last year Anhui officials inspected rivers and streams in 71 places. Of the areas tested, 45 were found to be grade four or worse (China grades water purity on a scale of one to five, with grade five being fit only for irrigation). In two of the province's rivers, 2,000 tonnes of fish died last year because of pollution. Officials admit that in Anhui, as indeed in the rest of China, the problem is getting worse, despite a few trumpeted improvements.

One of the proclaimed successes concerns the Huai, the country's seventh-longest river, which flows through Anhui. About 150m people depend on the river and its tributaries for their drinking water. At least until the mid-1990s, it was the country's most polluted large river system. A surge of pollution in 1994, caused by the simultaneous release of water that had been stored up in the Huai's tributaries during the dry season, caused tens of thousands of people along the main river to fall ill. Since then the Huai has been the object of a clean-up supervised by the central government, the first in China aimed at dealing with an entire river system.

The State Environmental Protection Bureau announced this year that its five-year anti-pollution campaign on the Huai had met its targets, and that in most areas the water was grade three, in other words fit to drink after treatment and boiling. In Huainan, a city in the middle reaches of the Huai, officials proudly show off their pollution-control facilities. The city says that by rigorously enforcing regulations it has succeeded in reducing industrial pollution to well within acceptable bounds, but that pollution caused by untreated sewage is still beyond the permitted limit.

But Huainan is neither representative nor especially admirable. Last year reporters from the official Xinhua news agency conducted interviews along the Huai's tributaries, discovering foul-smelling oily black water, dead fish and polluted wells. The agency reported that water tables were rapidly falling because of the frantic search for clean water underground. It said that downstream of Anhui, in Jiangsu province, pollution in the Huai itself had caused more than $25m of damage to crops in 2000 and affected the drinking water of 2.4m people.

The drought is not helping. Less water means higher concentrations of pollutants. But the underlying problem will not ease when the rainy season begins. A place such as Huainan can meet targets because the worst offenders in its area are state-owned enterprises (mostly chemical factories) which have to obey orders from the local leadership. Far more difficult to control are the thousands of smaller factories that have sprung up in the Huai River basin in recent years, many of them highly polluting paper mills and dyeing and tanning plants run by towns or villages.

In the coming years the task of cleaning up China's rivers will become ever more arduous. As the central government's powers weaken relative to those of the provinces, it will become increasingly difficult to enforce measures that threaten local economic interests. With economic growth outpacing that of tax revenues, it will be almost impossible to persuade bankrupt local bureaucracies to forgo the temptation of quick, environmentally damaging, profits.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Indonesia

Who's in charge?

Jul 19th 2001 | JAKARTA
From The Economist print edition

Will President Wahid or parliament blink first?

WILL he, won't he? Can he or can't he? President Abdurrahman Wahid kept Indonesia on tenterhooks this week about whether he would order a state of emergency, his draconian answer to efforts to unseat him. He had threatened to do so at 6pm on July 20th if no compromise had been reached by then in the long battle with parliament to end his presidency in mid-term. Mr Wahid also threatened to dissolve the legislature and call elections.

AP

Wahid heads for a showdown

The day before the deadline, Mr Wahid appeared to be backing away from the idea once again. A presidential spokesman said it might not be needed as efforts were under way to find a compromise. There were meetings with two of his chief opponents and talk again of a ceremonial role for the blind president as "father of the nation". Mr Wahid said the threat still stood, but that it might not take effect until July 31st, to allow time for a solution.

The vice-president, Megawati Sukarnoputri, Mr Wahid's presumed successor if he is ousted, made it clear she still favoured impeachment. His arch-enemy, Amien Rais, speaker of the People's Consultative Assembly (MPR), summoned its members to the capital, Jakarta, to be ready for a "snap impeachment" on the night of July 20th if need be. An aide of his said Mr Wahid would be "immediately impeached" if he issued his decree.

But does Mr Wahid have the power to dissolve parliament anyway? Adnan Buyung Nasution, a prominent lawyer, said that, should he try, Mr Wahid might end up on trial like the ousted Philippine president, Joseph Estrada. The charge would not be corruption, but treason. Mr Nasution is a name to conjure with in the Indonesian legal world, as deputy chief of the supervisory committee for the 1999 election and head of a legal team helping General Wiranto, a former military chief, in the matter of alleged atrocities in East Timor.

Mr Wahid is on shaky legal ground. He has sworn again and again to defend the 1945 constitution. But nothing in that constitution or elsewhere gives him authority to dissolve the legislature. In fact, its second article states that "sovereignty is in the hands of the people, and is implemented in full by the People's Consultative Assembly." The MPR appoints the president, not the other way around. His decree would presumably have to be based on an authoritarian 1959 law on emergencies, not exactly the tool of a democrat. A new statute was passed in 1999 but prompted bloody protests on the streets of Jakarta within hours. Several people died, and it was never signed into law.

Unfortunately, there is a historical precedent for Mr Wahid's proposed action, and it is not a good one. On July 5th 1959 Indonesia's founding president, Sukarno, issued a decree dissolving the Konstituante, a constitution-making body that had failed to achieve its goal in four years. It was the start of nearly four decades of dictatorship or near-dictatorship, first under Sukarno and then his successor Suharto.

Dewi Fortuna Anwar, an adviser to a former president, B.J. Habibie, says there was really no constitutional basis for that decree either. However, it was accepted because of the critical problems facing the country then, with rebellions in several regions. And it had the support of the armed forces, which Mr Wahid does not.

Indonesia's legal system, however, is a mess and almost everything involving the constitution is open to conflicting interpretations. In the views of those legal experts on Mr Wahid's side, if he declares an

emergency he can in theory do anything he likes. But in the world of realpolitik, without support from the soldiers and policemen who would have to implement the state of emergency, it would not work.

Insiders say Mr Wahid realises this. But should he decide, early on Friday morning, to back down, he may feel he is left with no alternative but to employ his final weapon: the fanatical mobs of his native East Java, who revere him like a saint and may descend violently on the capital to defend him. The losers in this would be first Mr Wahid himself and then his country.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

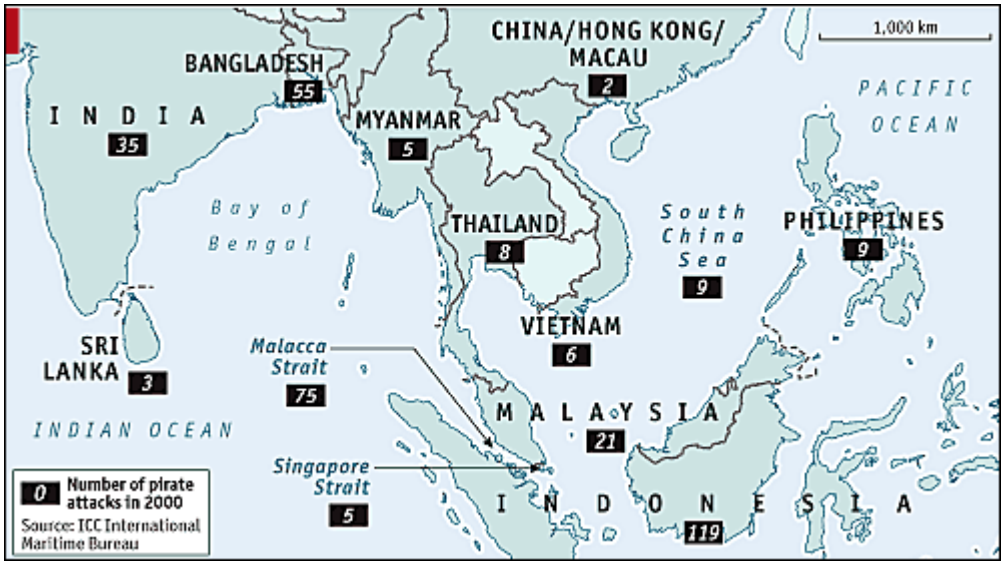
About sponsorship

Piracy in Asia

Dangerous waters

Jul 19th 2001
From The Economist print edition

Regional efforts to combat piracy are taking shape



SHORTLY after the *Selayang*, a Malaysian tanker, left Port Dickson in the Malacca Strait last month, she was boarded by pirates who took her crew hostage and re-routed her round the southern end of Borneo. After a week-long chase, Indonesian air and naval units eventually recaptured the ship. Luckily, all 14 crew members were unharmed and most of the ship's cargo of oil was intact. The crew of the *Cheung Son*—shot and thrown overboard when the ship was hijacked in the South China Sea in 1998—were not so fortunate.

Piracy is a growing threat to ships and their crews. The International Maritime Bureau (IMB), a division of the International Chamber of Commerce, reported over 460 attacks by pirates worldwide in 2000, an increase of 56% over 1999. And the International Maritime Organisation (IMO), based in London, estimates that only half of the incidents are actually reported. Attacks range from petty theft by unemployed fishermen and opportunistic criminals—the great majority of incidents—to highly organised, gang-operated hijacking.

Although there is growing competition from the seas that wash Bangladesh and India, the favourite pirate zone remains Indonesia's waters and in particular the Malacca Strait, which altogether account for over 40% of the reported attacks. The strait is one of the busiest waterways in the world, used by 200 or more ships daily. As they slow down, and lose their ability to manoeuvre in order to negotiate the narrow and shallow waters, cargo ships are sitting ducks.

In the mid-1990s, Indonesia, Malaysia and Singapore, the three states bordering the strait, appeared to have the situation under control, with only a single incident reported in 1998. But in 2000, 75 ships were attacked there. According to the IMB, Indonesia's deteriorating economic and political situation is at the root of the increase in piracy in the region.

Legal loopholes are also to blame. Most Asian countries do not have adequate national laws on piracy, though those that have treated it as a serious problem have made significant progress. Since China sentenced the 13 hijackers of the *Cheung Son* to death in 1999, pirates have been going farther afield to dispose of hijacked ships and cargoes. To help countries fill this legal vacuum, the Comité Maritime

International (CMI), a body of national maritime-law associations, has been drafting a model national piracy law, which should be ready by the end of the year.

National efforts, however, can extend only as far as territorial waters. When pirates make sail for neighbouring countries with their hijacked prizes, matters get more complicated. Some countries have had trouble investigating crimes that have been committed neither in their jurisdiction nor by their own nationals. When the Chinese authorities recovered the *Global Mars*, which had been hijacked near Malaysia last year, they had to let the crew—from the Philippines and Myanmar—go. Only five Asian countries (China, India, Japan, Pakistan and Sri Lanka) have ratified the IMO's 1988 Rome convention, which provides an international legal framework to chase, prosecute and extradite pirates.

Efforts to enhance regional co-operation have been multiplying. Besides pushing for more countries to ratify the convention, the IMO has developed a common code of practice to investigate crimes on the high seas, which it hopes will be adopted during its meeting next November. Japan, anxious to secure its maritime lifeline, has also been pushing for more active collaboration. The IMB's Piracy Reporting Centre—based in Kuala Lumpur—monitors ship movements around the world and co-ordinates pirate chases across borders. A few weeks ago it also brought together national authorities, marine policymakers and ship-owners in Kuala Lumpur. If countries in the region take these efforts seriously, the pirates could be the ones in dangerous waters.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Japanese reform

Sinking, not flying

Jul 19th 2001 | OSAKA
From The Economist print edition

The building of Osaka's new airport is burdened by bureaucracy

THE sea wall is built and the giant barges are swinging lazily into place, dumping their cargo of earth and rocks into the water. Building a second runway at the Kansai international airport, perched on a man-made island in the bay of Osaka, Japan's second city, has not been easy. Airport officials have battled grimly against hostile public opinion, campaigning local politicians and budget planners at the Finance Ministry, which keeps an anxious eye on the airport's ugly finances. At last, however, the sight of all that soil sinking into the sea has begun to lift their spirits. Only a severe earthquake, say airport officials, can stop their plans now.

Don't mention global warming

The celebrations may not last. Suddenly, there are new worries at "mini- Kasumigaseki", the airport's six-storey administrative offices, named after Tokyo's bureaucratic district because of its hundreds of government officials. Junichiro Koizumi, Japan's reform-minded prime minister, says he wants to take on his country's mighty bureaucracy. His targets are the myriad public-sector companies, called special corporations, whose business interests have spread into everything from mortgage loans to motorways.

Mr Koizumi has already claimed one scalp, the Japan National Oil Corporation, whose accumulated losses, from financing nearly 300 failed or failing oil-exploration ventures, may run to $10 billion or more. In the autumn, say Mr Koizumi's officials, the oil company will be divided and privatised. Officials at the Kansai airport must be wondering if they are to be next.

The company that runs the airport is a special sort of special corporation, called a "third-sector" project. The idea of these projects, born in the late 1980s as a wave of privatisations swept Britain and then other countries, was to improve public-sector efficiency with private-sector money and management. At Kansai, this principle was not so much lost as never discovered. Almost all the company's shares are owned either by the national government or by a consortium of five local governments. Its borrowings are guaranteed by the government. Most of the company's 500-odd staff are government workers on secondment. Most of its board members are former government officials.

Shoddy management has hobbled the company from the start. The airport is built on a type of clay whose behaviour, under a heavy load, is hard to predict. When the management asked its scientific advisers how much the island would sink into the bay, says Koichi Akai, who chaired the scientific committee, the scientists came back with a wide range of possibilities.

The managers chose the most optimistic estimate, and built their island and the company's finances on the hope that they would be lucky. They were not, and more soil and more loans were needed. The extra soil made the island heavier, so it sank even deeper into the mud. Although the airport opened in 1994, it is still sinking today, and Mr Akai reckons it may have another metre to drop. The extra soil, together with building work to protect fuel tanks and the terminal building have added $4 billion to costs, putting the first phase of the project about 50% over budget.

Flights to and from the airport did not match the company's sunny forecasts, and its losses started to mount. If the airport went ahead with phase two and built a second runway, it soon became clear, its finances would collapse. The solution, in the minds of the Transport Ministry's creative bureaucrats, was to establish a second airport company. This second company has borne the new runway's huge

construction costs, partly financed, this time, with subsidised, interest-free loans from the government. The second company will lease the runway to the first company when it is ready for use, in 2007. The first company will then buy the runway from the second company after a further 30 years, and the second company will be duly wound up. Thanks to a ten-year holiday on the debt, no one has to pay anything until 2007.

But not even these arrangements have satisfied the Finance Ministry that the airport's finances will improve. Last summer the ministry floated the idea that the project should be scrapped. Fierce lobbying put a swift stop to that, but the Finance Ministry still insisted on another financial restructuring. The plan, due to be unveiled at the end of August, will centre on converting yet more bank loans into subsidised, interest-free debt. At a meeting last month the airport's shareholders once again reappointed the management.

It is attitudes like these that Mr Koizumi must change if he is serious about tackling his government's sprawling commercial interests. Officials work within a tradition of all-powerful bureaucracy, and their contempt for the humble citizen is boundless. Yet the Japanese are not fools. "Japan is sinking," says a middle-aged man as the airport train rumbles over a 5km bridge towards the island, "just like this airport." What delight there would be in Osaka if Mr Koizumi left the airport standing, but buried its management.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Israeli-Palestinian fighting

Prospects of war

Jul 19th 2001 | JERUSALEM
From The Economist print edition

The ceasefire between Israel and the Palestinians is threadbare, even if full-out war is avoided

Get article background

AS ISRAEL'S tanks encircled Bethlehem at mid-week, suspicions were reawakened that its army could be laying out a contingency plan for an all-out assault on the Palestinian Authority (PA). Israel denies this, insisting that however vigorous its military actions—including the helicopter rocketing of Palestinian targets, tank fire and incursions into Palestinian territory—it is still only responding to, or pre-empting, Palestinian attacks. But after Monday's suicide-bomb in Israel, which killed two Israeli soldiers, Israeli talk of "self-restraint" has subsided and the right is pushing for war. Whatever the political intentions, events on the ground are in danger of forcing the issue.

Despite strong pressure from their militants, both the Israeli government and the PA are trying to avoid full-out war. But war is the temper of the moment. In one of the worst weeks of the *intifada*, the Israeli army laid siege to Palestinian towns and villages, commandeered Palestinian homes and snatched "wanted" men from PA-controlled areas. Tuesday's killing by helicopter fire of four Palestinians (including two leaders of the Islamic Hamas movement) was said by the Israeli army to be to prevent a "major terror attack" in Israel proper, with the target perhaps the closing ceremony of the Jewish Olympics taking place in Jerusalem. Palestinians said the four were at a party for a friend just released from an Israeli jail.

In response, and for the first time in the West Bank, Palestinian gunmen pitched two mortar bombs at the Jewish settlement of Gilo in occupied East Jerusalem. Earlier, Hebron, a divided West Bank city, had been shaken with violence after the killing of two Jewish settlers by Palestinian guerrillas on July 12th. Over the next five nights Israeli tanks twice rolled into the town, and battles raged between them and lightly armed Palestinian fighters. Over 100 Palestinian civilians were injured (including a dozen children), and Jewish settlers set Palestinian farmland ablaze.

"It's a systematic war, daily and incremental and debilitating," commented Hanan Ashrawi, a Palestinian spokeswoman who now also speaks for the Arab League. "It's an attempt to put into effect a war plan by an occupying military force against an occupied people without the negative responses that would accompany any kind of sudden or dramatic escalation."

Escalation, and its negative responses, have been dominating Israeli politics—as has the question of whether Ariel Sharon, the prime minister, or Shimon Peres, his foreign minister, is running Israeli policy. The two insist that they see eye to eye. But Mr Sharon is urged by his hardliners to respond more fiercely

to Palestinian attacks than Mr Peres would countenance.

Just hours before the latest suicide bomb, the prime minister invited his Labour Party colleague to the lion's den of his Likud parliamentary faction. The right lashed out at Mr Peres. "You're a diplomatic pyromaniac, our children are being murdered because of your pyromaniacal theories," one Knesset member yelled. It was a scarcely disguised critique of the prime minister himself. "We brought Sharon to power and instead got Peres as prime minister," is now a popular refrain among Jewish settlers in the West Bank.

Mr Peres seems to have been successful in persuading Mr Sharon to calm his personal attacks on Yasser Arafat. Only a couple of weeks ago, Mr Sharon was repeatedly calling the Palestinian leader a "bin Laden" with whom it was impossible to do business. "Why does your father talk about me like that?" Mr Arafat complained to Mr Sharon's son, Omri, when the young man was sent at the end of last week to Palestinian headquarters in Ramallah to press for de-escalation. To his satisfaction, he was told that the prime minister would no longer denigrate him as a "terrorist".

But if Mr Sharon and Mr Peres have agreed, at least for the time being, to stop trying to delegitimise Mr Arafat, and to maintain his credibility as a future negotiating partner, what hope is there of such negotiations taking place? The answer, at this point, is virtually none.

At a meeting with Mr Arafat in Cairo on July 15th, Mr Peres was partially successful in convincing his Egyptian hosts that neither he nor Mr Sharon had an interest in a general conflagration. But after the meeting, President Hosni Mubarak said flatly that there was no prospect of peace so long as Mr Sharon remained in power. And on these prospects, and the renewal of talks, Mr Peres has shown that he no longer takes issue with his prime minister. He too has begun to adhere to the strict Sharon maxim that there can be no resumption of political negotiations until all violence is ended entirely. Violence on the Palestinian side, that is: Israel does not include acts, such as the demolition of Palestinian houses or the undercover assassination of Palestinian targets, as violence.

Israel insists on seven days of absolute Palestinian quiet before any move can be made towards implementing the political ingredients of the Mitchell commission's proposals, and thus haul the conflict back towards negotiations. That was the upshot of last month's unprepared, and in the end counter-productive, mission by Colin Powell, America's secretary of state. Yoel Markus, a columnist on *Haaretz*, put it pungently: "The Bush administration... made Sharon the presiding judge in a case in which he himself is one of the parties before the bench." Mr Peres, no less than Mr Sharon, accepts this predicament.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Egyptian unemployment

Summer of fury

Jul 19th 2001 | CAIRO
From The Economist print edition

Egypt's growing pile of woes risks spontaneous combustion

Get article background

IN MOST places with raging unemployment, news that the government is hiring 170,000 people would be a cause for joy. In Egypt last week, the announcement sparked protests that left dozens injured. Tempers were shortened, and not merely because of the country's fierce summer heat, chronically stale politics and floundering economy. The mass job offer, it turned out, was aimed only at recent graduates, leaving thousands of older bureaucrats-in-waiting in the lurch. Stunned by their fury, the government hastily scrapped the age limits. This cooled public rage, but did little to deal with the root problems that make Egypt prone to such outbursts. Nor did it ease the impression that the country's ageing and authoritarian leaders are increasingly out of touch.

The anger of the would-be public servants was understandable. Some have been waiting for jobs since 1985. That was the year the government quietly began to disregard a 1950s-era guarantee of state employment for every university graduate. It had to: the state's overstaffed offices, factories, schools and police already employed a third of the workforce.

Hiring restraint and privatisation over 15 years have reduced that proportion to one in four, yet that still leaves some 6m Egyptians on the state payroll. Government planners had hoped that a shift towards market economics would spur enough growth to soak up the 800,000 people who join Egypt's job market every year. They were right, for a time, but a two-year slump has tipped unemployment to crisis levels.

Sketchy official statistics claim the figure is about 9%, but independent economists reckon unemployment is twice that, and growing fast. The untidiness of Egypt's economy, with its armies of vendors, servants and day labourers, helps disguise the scale of the problem. But the dearth of decent jobs means that advertisements for even the lowliest government positions bring avalanches of applications. Millions of holders of paper degrees, products of an education system geared towards volume rather than excellence, will accept wages of $50 a month, plus job security, rather than risk their chances on the street.

To its credit, the government has invested heavily in make-work projects and micro-financing. Yet the government appears keener to contain unemployment as a security threat than to release the economic potential that might actually solve the problem. Momentum for privatisation, for example, has all but died due to concerns about layoffs. This leaves Egypt with such burdens as a state steel concern whose 25,000 workers produce less than private plants with a tenth of the workforce, and a state broadcasting monopoly with over 30,000 employees, whose shoddy productions are rapidly losing out to satellite broadcasts from abroad.

Aside from promising more jobs in the wake of last week's unrest, the government took the opportunity to arrest 25 members of the Muslim Brotherhood. Though officially outlawed, the group is the only credible opposition force in parliament. Brotherhood sources believe the arrests may presage a wider crackdown.

President Hosni Mubarak also abruptly replaced seven provincial governors, mostly with men plucked from the top ranks of the army and internal security forces. The action, unusual for a president renowned for his cautious aloofness from administrative matters, seemed to reflect a determination to impose discipline. Many see it, however, as a sign of frustration.

The president and the unemployed are not the only Egyptians frustrated by the government's

performance. Since being installed two years ago amid a hail of criticism against its predecessor, the cabinet chaired by the prime minister, Atef Ebeid, has limped from crisis to crisis. Summing up Egypt's black mood, Mustafa Bakri, the maverick editor of a tabloid newspaper addressed a plea to Mr Mubarak. "We're suffocating, Mr President. We want to breathe again, Mr President."

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

African unity

Gadfly Qaddafi

Jul 19th 2001 | LUSAKA
From The Economist print edition

Few disagree with the Libyan leader's pan-African plan

Reuters

MUAMMAR QADDAFI has been buzzing around Africa recently like a frantic bee. Last week he was pressing his ideas for the unification of the continent at the African leaders' summit in Zambia. Then he, his female bodyguards and a motorcade 80 cars long, swarmed to Zimbabwe to witness its fuel shortages. This week he was in Uganda, making a new friend, a boy king, and visiting Yoweri Museveni, the president, an old friend.

Why this Afro-enthusiasm? Dictator of Libya for more than three decades, Mr Qaddafi would now like to be something far grander: president of all Africa maybe? He has been pushing his pan-African credentials for several years, even though his pan-Arab plans have come to naught. But he is particularly active now. An attempted coup in May in the Central African Republic was put down with the help of Libyan troops and combat helicopters.

That same month Mr Qaddafi persuaded Sudan and Uganda to restore diplomatic relations, as a step towards peace talks to end their proxy war. Before the Organisation of African Unity (OAU) met in Zambia's capital Lusaka this month, the colonel paid off the debts owed to it by some small West African states. Some diplomats muttered darkly about Libya's "unprincipled" activities. But most African leaders find it pays to agree to whatever the Libyan Brother Leader suggests, because he hands out cash generously to friends. If they do not agree with him, their enemies get the cash. In Lusaka the cash flowed freely—even foreign journalists were offered bundles by Libyan officials.

Colonel Qaddafi's foreign jaunts and bribes have produced results—at least in name. The moribund OAU has been reborn as the African Union. Speakers lined up in Lusaka to herald the unification of Africa. Some said the African Union would be just like the European Union.

However, unlike Europe when the EU was founded, much of Africa is still at war. The most exuberant supporters of the African Union say that peace will break out when Africa's borders disappear. African conflicts "philosophically and historically expose the unity of Africa," claims Colonel Qaddafi, with unfathomable logic.

Plans are already afoot to give the union institutions. Mauritius has volunteered to play host to an African court of justice. Colonel Qaddafi gallantly offered to house the continent's parliament, but since he does not allow one for Libya, this was turned down. Some suggest that Africa should have its own central bank and currency—the "afro", joked Tito Mboweni, South Africa's central-bank governor.

Most Africans and their leaders like the dream of unity but their record of political and economic organisation at national or regional level suggests it will remain just that, a dream. The political commitment and the money to make it come true are not there. And when Colonel Qaddafi begins to talk of his African vision, more serious leaders fall back in horror. He speaks of "going back to an Africa before colonialism, an Africa of tribes and kings". That may interest his young Ugandan monarch friend but appals leaders who want a modern Africa. They also ask why, if the colonel preaches peace and unity, he supported Liberia's war in West Africa. Libya's invasion of Chad in 1980 is also remembered by black Africans, as is the mass expulsion of West African migrant workers from Libya last October, after black African immigrants had been attacked by mobs and at least 150 people killed. Not exactly an action that reflects the borderless Africa Colonel Qaddafi claims to want.

The danger is that his grand scheme will draw attention from a more serious plan by South Africa's president, Thabo Mbeki, and supported by Egypt, Senegal, Algeria and Nigeria. It promotes good government, freer trade and economic growth. Unlike the colonel's dreams, this could actually improve the lives of ordinary Africans.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Burundi

Doubtful peace

Jul 19th 2001 | KIGALI
From The Economist print edition

The latest peace agreement looks good but not many Burundians believe in it

LED by Nelson Mandela, the international acclaim for an agreement signed last week in Pretoria suggests that the political deadlock in Burundi has been broken and eight years of civil war may be over. Few Burundians think so.

All the 19 parties that signed an accord in Arusha, in Tanzania, last year have now agreed—at least on paper—who should be the boss. For the first 18 months of a three-year transition period the country will be led by President Pierre Buyoya, who came to power in a coup in 1996 and is Tutsi. During this period, a Hutu leader, Domitien Ndayizeye, will serve as deputy president and the two will switch roles for the second half of the transition period. A starting date will be worked out at a meeting of all parties on July 23rd in Arusha.

Many observers think the sudden willingness to compromise in Pretoria is just a façade. “They’re all playing games; they’ll go back and camp stubbornly on their previous positions,” says one. This is a hard war to bring to an end. It does not have a front line or two well-defined opposing groups. It is full of paradoxes and crossovers. For example, a senior member of the National Assembly is the brother of the leader of one of the country’s two main rebel groups. Rebels attack villages, steal cattle and burn houses but spare the homes of their relations.

Neither side can win. The sympathy of the Hutu majority lies firmly with the rebels, so there is little chance that the Tutsi-led army will ever destroy them. On the other hand, the rebels stand no chance of overthrowing the government. The whole region seems set for a war of attrition between the beleaguered but well-armed Tutsis in power and the more numerous and resentful Hutus.

The new accord, negotiated by Mr Mandela, has the same shortcomings as all the other failed agreements. First, only unarmed parties have signed. The accord excludes the country’s two armed rebel Hutu groups: the Forces for National Liberation (FNL) and the Forces for the Defence of Democracy. The FNL immediately said it was not bound by the agreement and pledged to fight on.

President Buyoya is not known for compromise either. This agreement leaves him in power for the moment and gives him a smooth, face-saving exit. He has been disavowed by both Hutus and Tutsis. He is associated in the minds of most Hutus with the attempted coup that overthrew the first democratically elected Hutu president in 1993. Most Tutsi parties, on the other hand, consider Mr Buyoya too willing to compromise with the Hutus.

The agreement also fails to take account of the neighbours: Rwanda, Tanzania and Congo. Small and landlocked, Burundi depends heavily on them, but its civil war has extended into their territory and politics. Tanzania has half a million Burundian Hutu refugees encamped on the border. Its government is so divided over Burundi that the president, Benjamin Mkapa, will not take a firm stand. Many members of his cabinet want justice for the Hutus. Others just want peace in Burundi. Some are indifferent. Hutu rebels can easily infiltrate the camps in Tanzania and use them as a base for attacks on Burundi.

The Rwandan government, militarily strong, believes that whoever is in power in Burundi will have to co-operate with it. Rwanda watches its “twin” closely, more so now that infiltrators from Congo are heading

back into southern Rwanda via Burundi. The Rwandans fear that anti-Tutsi sentiment in both countries could bring their rebel movements together.

Burundi's war is also inextricably linked to the war in Congo. As President Joseph Kabila comes under increasing pressure to stop supporting rebellious exiles from Rwanda and Burundi, he appears to be pushing both groups eastwards. Thousands are reported to be heading for Burundi from the south-east. Soon they will be clashing with Burundi's notoriously chaotic army. Any fighting will be nasty but not militarily decisive, and will make the peace accord look irrelevant.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Greece's threatened reforms

A need to clear the air

Jul 19th 2001 | ATHENS
From The Economist print edition

Costas Simitis, a modernising prime minister, must fend off a challenge

TWO summers ago, thousands of Greek holidaymakers were glued to their mobile telephones, checking prices and trading shares as they lounged on the beach. As the stockmarket soared, ministers in Greece's centre-left Pan-Hellenic Socialist Movement, better known as Pasok, delightedly claimed credit for having launched popular capitalism.

AP

Simitis needs a firmer hand

More recently, the Socialists have been changing their tune. After falling for months, the stockmarket on July 16th hit a three-year low. Small investors, the worst hit, feel wretched. Stockbrokers who let favoured customers buy shares on credit face bankruptcy. Last year the government used some cash from privatisation sales to prop up the market. But as a member since January of the euro club, Greece is obliged by European Union rules to spend its spare cash slimming the bloated public debt.

No wonder Costas Simitis, the prime minister, is feeling the heat. One polling company says his approval rating has sunk below 30%, his lowest ever. Most voters seem to think that Costas Karamanlis, the untested leader of the conservative opposition, would do a better job. Dissatisfaction with Pasok, in power for all but three of the past 20 years, is running high.

After five-and-a-half years as prime minister, Mr Simitis, an ex-academic fond of hard work and detail, is under fire from some former supporters. Businessmen, less cowed than in the past, want him to move faster with liberalising the economy. Lumbering state enterprises still dominate telecoms, transport and power production. Taxes are high and paying them is a complicated and time-consuming affair.

Mr Simitis is clearly rattled. Though a dedicated reformer, he shelved plans to overhaul the decaying pay-as-you-go pension system, after public-sector unions, his power base in Pasok, held demonstrations in protest against even the modest reforms he had proposed. Despite pressure from Brussels, the timetable for preparing a new pension law is vaguer than ever.

Mr Simitis fought back by insisting that Pasok's next congress should be in October, six months earlier than planned. He will stand for re-election as the party leader. But he may be opposed.

George Papandreou, the foreign minister and son of Pasok's populist founder, the late Andreas Papandreou, would be the best-qualified alternative. He would have a better chance than most to unite the party's two main factions: its old-fashioned tax-and-spend populists and pro-euro modernisers. So far, though, he has proved a loyal member of the modernising faction. He is ready to wait, telling friends he has plenty of time to bid for the leadership in the future.

Not so Akis Tsochatzopoulos, the ageing defence minister who leads Pasok's populists. Despite two defeats at the hands of Mr Simitis for the top job, he would still like to be prime minister. The October congress could be his last chance for revenge.

The betting is still on Mr Simitis. But simply winning would not be enough. He has to win handsomely to shut the populists up while he forges ahead with reforms. If not, the achievements of the past few years—low inflation, faster growth than the EU average and an acceptably low budget deficit—could be reversed. Greece's hopes of emulating Portugal and Spain, both now looking forward to ever-greater

prosperity through their membership of the EU, would then start to fade.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Portugal's politics

Guterres stumbles

Jul 19th 2001 | LISBON
From The Economist print edition

The prime minister parades his achievements. Voters are not impressed

FULL employment, poverty alleviated by a minimum guaranteed income, lower taxes, membership of the euro, 700,000 new home-owners, nursery schooling for all, an 80% rise in the lowest old-age pensions, a big increase in university places. Antonio Guterres, Portugal's Socialist prime minister, reeled off an impressive list of achievements in a television interview last week. Alas for him, the popularity of soap operas and "reality" shows meant that Mr Guterres managed to draw only 8% of the national audience.

His appeal to voters is not much better. Opinion polls show his Socialist Party behind the opposition Social Democrats, the main party of the centre-right, for the first time since he led his lot back to office in 1995. Among a panel of 98 top businessmen, 86 rate his performance over the past three months as "poor" or worse.

Disgruntled ex-ministers—a body that is ever growing—are as caustic as opposition leaders. They accuse Mr Guterres of weak leadership. He has shied away from difficult decisions and set no goals for the country to aspire to, they say. To the opposition's delight, Joao Soares, the mayor of Lisbon, last week became the first prominent Socialist to break ranks and suggest that a general election two years ahead of schedule would clear the air. Is the man who modernised the Socialist Party, led an elated Portugal into the euro and personified a new mood of confidence, buoyed by low interest rates and strong economic growth, losing the plot?

His replacement of six leading ministers on June 29th left the impression that he was responding to opposition pressure rather then asserting leadership; it was a public-relations catastrophe, says Mr Soares. Nor is the economy helping. The Bank of Portugal has cut its economic-growth forecast for 2001 by half a point to 2.0-2.5%, down from 3.2% last year. The stockmarket is down by more than 20% since January.

The real causes of Mr Guterres's fall from grace, however, lie closer to the early-morning queues of people waiting to make appointments for hospital treatment that they will not receive for months, to the voters frustrated by the snail's pace of the court system, and to small businessmen who feel their initiative is being stifled by a creaking bureaucracy. Public services are failing. After years of Socialist power, Portugal's voters, unlike Britain's, are not to be fobbed off with excuses which blame earlier, rival governments or promises that all will be put right if only the people will have patience.

Nor should they be. Portugal's 10m people spend 15% of GDP, more than any other EU country, to pay an army of nearly 700,000 civil servants. Many are underemployed and unproductive, through little fault of their own. Yet pay in the public sector has risen far faster in the past 15 years than in the private sector, leaving it today, on average, some 45% higher.

Perhaps because state employees account for about 8% of the electorate, Mr Guterres has eschewed radical reform of the public administration. Indeed, the state has recruited more than 50,000 new employees since he took office. The slowdown in the economy, and therefore in tax revenues, has now forced him to promise a cut of *euro*750m ($640m, about 0.6% of GDP) in public spending this year and to announce a batch of long-term measures to restructure government spending.

Needed, no doubt, but not likely to win votes. If Mr Guterres this autumn cannot get a tight budget for next year through parliament, where his party is one seat short of an overall majority, he will probably have to face an early election, at a time when he will be ill-placed to fight one.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Italy's finances

Rocky road ahead

Jul 19th 2001 | ROME
From The Economist print edition

The economy minister blames his predecessor and vows to do better

POINTING smugly at a board with lots of figures on it, Italy's economy minister, Giulio Tremonti, went on prime-time television last week during the main news bulletin to warn his compatriots that they might have to tighten their belts a bit before enjoying the promised entrepreneurial fruits of Silvio Berlusconi's new centre-right government. At the top of the board was the caption: THE CENTRE-LEFT'S LEGACY. This year, Mr Tremonti explained, Italy's budget deficit would be between *euro*23 billion ($20 billion) and *euro*32 billion some 1.9-2.6% of the country's GDP, far more than the 0.8% that the outgoing government had promised to other euro members.

AP

Tremonti makes them tremble

Mr Tremonti's lecture lasted only a few minutes but caused the intended ructions, at home and abroad. The left fumed. Giuliano Amato, its last prime minister, rubbished Mr Tremonti's figures. Vincenzo Visco, the departed treasury minister (as Mr Tremonti's job used to be called), scolded his successor for trying to "terrorise the public".

So is there a big hole in Italy's public finances? The Bank of Italy's governor, Antonio Fazio, supported Mr Tremonti. But economists and bankers vary on the matter. Most agree that the deficit will be larger than projected; the dispute is over exactly how much larger.

Having duly noted the left's failings, Mr Tremonti this week began to soothe European and Italian nerves by unveiling a five-year plan that includes a promise to cut both taxes and public spending, each by 1% a year, and to balance the budget by 2003. This year's inherited goal of squeezing the deficit to 0.8% has not changed but will, says Mr Tremonti, be "terribly hard" to meet.

In any event, Mr Tremonti's own plan assumes that Italy's economy will grow by more than 3% for each of the next five years and that unemployment will fall from 10% today to less than 7% by 2006. Given that Italy has not grown that fast in any year during the past decade and that a world slowdown is under way, his projections look worryingly optimistic.

A better-founded hope is for the faster sale of state assets. That way, Mr Tremonti reckons he can raise some $54 billion in the next five years, leaving him with enough spare cash to embark on some of the grand infrastructure plans promised during the election campaign. Most daringly of all, he says his government will tackle Italy's vastly profligate public-pension scheme. If it succeeds in that, it would be a triumph indeed.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Europe's single currency

Trust or mistrust thy euro neighbour?

Jul 19th 2001 | BRUSSELS
From The Economist print edition

With less than six months to go before Europe's single currency is issued in notes and coins, strains are beginning to appear among the 12 countries in the euro-zone

THERE are things about Italy that have always made other countries in the euro-zone nervous. That traditionally carefree approach to public finance, those habitual devaluations of old, that huge public debt. So when the new Italian government recently announced that it was likely to run a much bigger budget deficit this year than its predecessor had promised its EU partners (see article), there was a sharp intake of breath in European finance ministries.

Within a couple of days the Italian economy minister, Giulio Tremonti, had come up with a plan that he said might allow him to hit the original deficit target after all. But that may have only calmed matters for the moment. Many in Brussels are not convinced by the Tremonti plan. They fear that by the end of the year it will be clear that the Italians have indeed broken through the agreed deficit limits. At that point, just a month or so before the launch of notes and coins, the European Commission would probably feel obliged to issue a formal reprimand to Italy.

The euro group has seen this problem coming for a while. When the commission controversially rebuked Ireland earlier this year—for cutting taxes in the middle of a boom—many eurocrats said *sotto voce* that the real point had been to send a signal to Italy that the euro club was serious about holding its members to their promise to run fiscal policies that reflected the general European interest. Indeed all euro countries have signed up to a German-inspired "stability and growth pact". This states that any country in the euro-zone that runs a fiscal deficit of more than 3% of GDP could be subject to huge fines of up to 0.5% of GDP. As well as agreeing to this draconian procedure, club members have agreed to maintain budgets that are, in normal times, "close to balance or in surplus". The EU's latest guidelines foresee all euro countries achieving this goal by 2004.

The authorities behind the euro, in the commission in Brussels and in the European Central Bank in Frankfurt, think it is crucial to the credibility of their fledgling currency that the countries that adopt it should be seen to stick to these commitments. But some argue that the rules make little sense. By joining the euro, national governments have already given up two traditional tools for managing their economies—their unilateral ability to vary interest rates and to devalue their currency. Critics say that euro-zone governments should in consequence have been allowed maximum freedom to use their remaining tool—fiscal policy. After all, if a government like Italy's were to abuse that freedom, by running up unmanageable deficits, it would be the Italians who suffered worst because the markets would charge

a risk premium for lending to Italy.

But defenders of the stability and growth pact disagree. They argue that big budget deficits in Italy or elsewhere might indeed have a negative “spillover effect” on the other euro members. The main problem they fear is that profligate countries would drive up the overall deficit of the euro-zone and spark inflation. That, in turn, would make it harder for the European Central Bank to lower interest rates. So the disciplined countries would pay an economic price for the spendthrift habits of the others. The commission also thinks that if Ireland and then Italy are “allowed to get away with it”, it will become ever harder to enforce fiscal discipline across the entire zone. One country running a lax fiscal policy is one thing. What if four or five did so at once?

And indeed, though the spotlight has fallen on Italy this week, it is not the only malefactor. In a recent report the commission singled out four countries in danger of breaching their budget-deficit promises: Germany, France and Portugal—as well as Italy. Awkwardly, that group includes the euro-zone’s three largest economies. The Germans, always the strongest advocates of fiscal discipline, now find themselves in budgetary difficulty because Chancellor Gerhard Schröder’s government is pushing through a bunch of tax cuts in the middle of an economic slowdown. The French, who were miffed to be lumped in with the bad boys, were fingered for not using good economic times to bring their budget back into balance.

The small size of the Portuguese economy means that its problems affect other euro countries less. Portugal, however, is a good example of how membership of the single currency can be a mixed blessing. The euro-zone already has a single interest rate, a lot lower than the one Portugal needs. Partly as a result, the country has experienced a credit boom and now has a current-account deficit of over 10% of GDP and the zone’s highest inflation. That in turn has fuelled bigger public spending and a rising budget deficit. Last month, in an effort to regain control, Antonio Guterres, Portugal’s prime minister, sacked his finance minister and then pushed through a batch of emergency budget cuts (see article).

None of the countries being urged to squeeze their deficits will be helped by the global slowdown that has now clearly spread to Europe. When economies are growing more slowly, tax revenues go down and social-security claims go up. But none of the strains within the euro-zone is unmanageable yet. No country is close to breaching the 3% limit, which would conjure up the nightmare of large fines being imposed by the commission in Brussels.

The real test of fiscal stability in the zone may come, not this year, but in around a decade’s time when baby-boomers are retiring and pension commitments begin to strain budgets across Europe. The European Commission now calculates that “public pension expenditure will rise by 3-5% of GDP in most EU countries over the next few decades”. But pushing through pension reform, to lighten this burden, is extremely hard. A recent effort by Greece’s government was put on ice after demonstrators filled the streets of Athens (see article) and Greek newspapers ran alarmist stories about “Brussels” forcing Greece to cut pensions.

That is just one anecdote. But it illustrates a big problem for all euro countries. How can they keep their promises to each other—and their voters sweet at home?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

German gays

Stronger-wristed

Jul 19th 2001 | BERLIN
From The Economist print edition

The German capital's next mayor is homosexual, and most Germans don't mind

"I'M GAY, and that's just fine," declared Berlin's acting mayor, Klaus Wowereit, as he accepted the Social Democrats' nomination to be their candidate in October to take the job for a full term. In a country where the two main opposition parties still have "Christian" in their names and where "protecting the family" is enshrined in the constitution, Mr Wowereit's candour was bold. True, Parisians had elected a professed homosexual as their mayor earlier this year, but surely the Prussian denizens of the capital of Hitler's homophobic Reich could hardly be likened to those free-thinking, fun-loving French?

Why not? Before Hitler came along, homosexuals and other nonconformists had long been drawn to Berlin's artistic milieu, exotic night life and relaxed social mores, especially after the first world war. And after 1945 "alternative" West Berlin was a magnet to pacifists, artists, hippies, gays and others dodging military conscription in the only part of Germany that was exempt from it.

Now Berlin is the nation's "gay capital" as well as, once again, its political one. This year over 500,000 people flocked to take part in Europe's biggest homosexual spectacle, the Christopher Street Day Parade—not to be confused with the city's yearly and mainly heterosexual Love Parade and its rivals, the Fuck Parade and the Erotica Carnival.

So if a homosexual politician were to stand a chance anywhere in Germany, Berlin would probably be the place to start. Pollsters guess that Mr Wowereit's honesty will lose him few votes. Over three-quarters of Germans say they would not mind having a gay mayor in their capital, two-thirds say they would accept a gay chancellor, and half claim they would not be put out if their own son or daughter admitted to being gay.

Still, notably few politicians have openly "come out". No federal minister has ever done so. Of the Bundestag's 666 current members, only three—all on the left—say they are gay. Yet at least a score are thought to be, half of them from the staunchly "pro-family" Christian Democratic Union and its more conservative Bavarian sister party, the Christian Social Union.

The centre-right opposition has been trying to block a law that would give homosexual couples many of the rights of married heterosexuals in such matters as inheritance, pensions, welfare benefits and immigration, though not tax or adoption. Granting legal weight to gay partnerships, say many right-wingers, would undermine the constitutionally protected family and even "promote decadence". But this week the Constitutional Court rejected such arguments, paving the way for the new law to take effect on August 1st.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

France's secret service(s)

Letters of cachet

Jul 19th 2001 | PARIS
From The Economist print edition

A rich variety of agencies watches over—or just watches—the nation

Get article background

WHY, over the course of each year, with the approval of its parliament, should France's government need some $50m in "special"—that is, secret—funds whose dispersal, much of it in crisp bank notes, is at the sole discretion of the prime minister? One embarrassing reason, as both President Jacques Chirac and the prime minister, Lionel Jospin, have come close to admitting, is to reward overworked ministers and officials in ways that the taxman need never know about. Indeed, Mr Chirac confesses that between 1992 and 1995, when he was merely mayor of Paris, he used special funds from an earlier stint as prime minister to pay for family trips abroad.

But another reason is to finance secret-service operations. This year some $30m of the special funds goes to one such agency, the General Directorate of External Security (DGSE). This is the body whose agents in 1985 were sent to stop the eco-activists of Greenpeace using their ship *Rainbow Warrior* to interfere with French nuclear tests in the Pacific. The ship ended on the floor of Auckland harbour in New Zealand with a bomb-hole in the side and a Greenpeace photographer dead.

Doubtless there have been other such operations to protect French national interests, though without such public repercussions. Unofficial sources talk of operations in Algeria, both during its bloody war of independence and more recently to protect French citizens from Islamic extremists; in Vietnam in the 1950s; in Libya in the 1970s; in Congo-Brazzaville in the 1990s. Recently a former Moroccan secret agent confirmed long-held rumours that French agents had been involved in the 1965 kidnapping, torture and killing in France of Mehdi Ben Barka, leader of the Moroccan opposition.

But how does France define its interests? Pragmatically and widely is the answer. In 1999 British Aerospace officials negotiating in Toulouse with their colleagues at Airbus Industrie found that documents had been filched from their hotel rooms by agents of the Directorate for Territorial Surveillance (DST), the internal counter-espionage agency. One reason why the French government, unlike backbench parliamentarians, has sung rather *piano* in the European chorus criticising Echelon, the electronic eavesdropping system operated by the United States, Britain, Canada, Australia and New Zealand, is that it has a similar system of its own.

Not that foreigners are the only ones honoured with the attentions of the gumshoes. Back in the early 1970s, the *Canard Enchaîné*, a Paris weekly that specialised in printing embarrassing official documents, caught a DST "plumber" busy planting a bug in its offices. Indeed—as in other countries, be fair—the secret services are widely believed to spy on each other.

Services, plural? Very much so: the DGSE and DST are just two in an alphabet soup of them. Besides the DGSE, the defence ministry has the DRM and the DPSD. The DST answers—though probably no more than it chooses to answer—to the ministry of the interior; so does the RG. And the prime minister's office has its own surveillance agency, the GIC. No wonder some 100,000 telephone lines a year are said to be tapped. One of those lines in the 1960s and 1970s no doubt belonged to a Trotsykite known as Comrade "Michel". Today he is known as Lionel Jospin.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD EUROPE
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Divided Cyprus

The danger of over-doggedness

Jul 19th 2001 | NICOSIA
From The Economist print edition

Rauf Denktash is asked to think again

A NEW argument is taking shape on the divided island of Cyprus. This time the Turkish-Cypriots are fighting not against their old enemies, the Greek-Cypriots, but among themselves. Some 6,000 Turkish islanders waving EU banners and chanting anti-Ankara slogans gathered last weekend in Inonu Square, in the Turkish bit of Nicosia, to protest against mainland Turkey's government—and against their own leader, Rauf Denktash. Some went so far as to liken him to Mussolini and Hitler. Others heaped praise on the Greek-Cypriot leader, Glafcos Clerides. The demonstration, large by Turkish-Cypriot standards, took place a few days before official celebrations on July 20th to mark the 27th anniversary of Turkey's military intervention on the island.

The veteran Rauf Denktash, who has led the Turkish-Cypriots for over 30 years, knows that a growing number of them disagree with his stubbornness in the talks about reuniting the island. He insists that everybody must recognise the sovereign separateness of the Turkish part of it before any deal is possible. His critics would sooner sit down and try to negotiate a loose confederation between the two parts of the island.

Ever since Turkish troops landed on it in 1974, when a coup by Greek-Cypriot extremists briefly threatened to make Cyprus part of Greece, the 200,000 or so Turkish residents of northern Cyprus—from which nearly as many Greeks fled after the invasion—have enjoyed peace and security. But, hit by an international embargo, they have also grown a lot poorer, while the internationally recognised Greek-Cypriot part of the island has grown much richer, and will do even better if its application to join the EU succeeds. The Turkish-Cypriot part has stagnated. Turkey's five-month-old financial mess has made matters worse. Embarrassingly for Mr Denktash, at least 2,000 Turkish-Cypriots are said to have applied for Greek-Cypriot passports in the past two months.

Mustafa Akinci, leader of the liberal Communal Liberation Party, wants less interference from Turkey in the island's affairs. In May this cost him his job as deputy prime minister in the Turkish-Cypriot government. A newspaper critical of Mr Denktash, *Avrupa*, has been hit by a bomb.

Mr Denktash has accused advocates of a Greek-Turkish dialogue of being "spies on the payroll of foreign diplomats"—and has recently said he has evidence to prove it. A group called the National Action Movement, which goes around villages reminding residents of atrocities committed by Greek-Cypriots before 1974 and heaps praise on "our saviours from the Motherland", is said to have been conceived by Mr Denktash and his mentors in Turkey.

Still, a growing number of mainland Turks also question the merit of leaving things as they are. If Mr Denktash agreed to resume the reunification talks, they say, the EU might delay Greek Cyprus's entry into the Union, a new Cypriot confederation might take shape, and everybody could be better off. The ground is wobbling under those dug-in heels.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Bulgaria's royal prime minister

The wrong job?

Jul 19th 2001 | SOFIA
From The Economist print edition

It may not have been wise of ex-King Simeon to become prime minister

CROWNS off to Simeon Saxe-Coburg-Gotha for becoming the world's first dethroned monarch to have won back power at the ballot box. This week, some 55 years after he was unceremoniously kicked out by Russian-run Communists as a boy-king only nine years old, he was asked by Bulgaria's president to form a government. Since his Simeon II National Movement won 120 out of the 240 seats in last month's general election, he should win a parliamentary nod of approval: the main opposition United Democratic Forces, a right-wing coalition whose biggest component is (confusingly) the Union of Democratic Forces (UDF), says it will not contest his nomination; and a party of ethnic Turks, with 21 seats, is set to join him in coalition. But how will the former king set about running the country? And will he, among other things, regain his crown?

Reuters

From king to exile to prime minister to...

The UDF, led by Ivan Kostov, a poor communicator, lost power because it was reckoned by most Bulgarians to be too corrupt. It had not, in fact, governed badly. After all, it took over in 1997 after the ex-Communists, who had come back to power in 1994 following a first botched attempt at reform by inexperienced free-marketeers, had all but bankrupted the country and almost caused a revolution in the streets. Of all the once-communist states buffeted by transition, Bulgaria was probably in the unholiest mess.

The UDF stemmed that tide of chaos. It managed to steady the currency; brought down inflation; saw the economy grow by an average of around 4% during its last three years in office; persuaded the European Union and NATO to accept Bulgaria as a serious candidate for both clubs; and kept the country out of Balkan imbroglios to the west (in Serbia, Kosovo and now in Macedonia).

But many—perhaps most—Bulgarians failed to see their standard of living return even to communist-era levels. Moreover, they loathed seeing well-connected crooks prosper apparently without Mr Kostov doing much to restrain them. That is why, in despair, they looked to their former king to fulfil his grandiose promise to make people better off within 800 days—and to clean the country up.

How? Mr Kostov on taking office made exactly the same promises to squelch corruption. Old ideas are being aired anew. The arrests of some of the biggest crooks may, it is thought, be exemplary. The revamping of the customs service is overdue. The privatisation agency may be overhauled. Far greater openness in selling state assets is pledged.

For sure, Simeon has a clutch of eager young bankers and accountants, some of whom have done well in Wall Street and in the City of London. "Our economic philosophy is much the same [as the UDF's]," says Milen Velchev, a 35-year-old Merrill Lynch man tipped to be finance minister, "but our policy [for implementing it] will be more radical." He reels off a list of measures he hopes to enact: abolishing taxes on profits reinvested in the company; lowering income tax gradually from a top rate of 38% to 29%; removing capital-gains taxes; letting foreigners buy land; and rapidly privatising the big companies that Mr Kostov funked selling off, notably telecoms, the tobacco monopoly, gas distribution, energy utilities and two big banks.

That sounds fine. But Bulgaria is, alas, still in thrall to a host of powerful and often criminal business interests, some with strong links to Russia. Mr Kostov wanted to sell off many of the same assets—but found that those interests were very hard to thwart. Indeed, their tentacles reached into parts of the UDF

that a few years earlier had sounded as keen as Simeon's lot now do to root out corruption.

The ex-king's integrity has not been questioned but his outfit will face the same pressures and temptations. For a start, it will have to turn itself into a proper party. Then it must decide how to deal with adversarial politics, despite its bid to be a movement for national unity. Formed only in April, it lacks organisation and hierarchy, beyond the iconic figure of the former king. And it probably lacks money.

"There's a mad rush to offer cash to the king," says a western banker in Sofia, the capital. Some companies with bad reputations have been angling for influence. Ilya Pavlov, who runs Multigroup, the country's biggest and most controversial conglomerate, once tied to Gazprom, Russia's giant gas company, is keen to befriend the king. Michael Chorny, a Russian-born metals magnate with a poor reputation, is thought still to be behind a newspaper that now lauds Simeon to the sky.

Though most of the returning western bankers and lawyers seem sincere and commonsensical, others who have the king's ear are less widely trusted. Stoyan Ganev, a former foreign minister in the early 1990s who may well run the king's office, is a friend of the Rev Sun Moon, a South Korean minister-cum-businessman. Other MPs in Simeon's movement have eyebrow-raising connections.

The ex-king himself remains enigmatic and aloof. "He is a good listener and gives free rein to his experts," says an economist in his team, admiringly. But Simeon will soon have to show that he can be decisive and even ruthless. No sign of that yet.

What about that crown, then?

It is unlikely that he intended to become prime minister. It was just that nobody else seemed to fit the bill. Now he will have to take the blame if improvements are not visible fairly soon—and if the crooks who have plundered the country retain or regain influence on high.

Had the ex-king stayed out of government, pulling strings from behind the stage, his chance of recovering the throne (an ambition he has not acknowledged but probably quietly harbours) was not bad. He might, if the constitutional court had allowed him, have had a good shot at winning the presidency when it came up for the voters' choice this autumn. Indeed, he looks rather well suited to being a constitutional monarch. But now he will be enmeshed in the grubbiest of party politics. It will be hard. In a year's time, perhaps earlier, he may look much less regal—and much less able to work miracles.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD EUROPE
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Charlemagne

Juan Jose Ibarretxe

Jul 19th 2001
From The Economist print edition

The premier of Spain's Basque region is looking for political progress, not trouble

Get article background

WHO would choose to be premier of Spain's bloodstained Basque region? For 2 1/2 years Juan Jose Ibarretxe was his party's choice for the job, treading a fine line between, on the one side, the separatist gunmen of ETA and, on the other, recently, the political bludgeoning of Spain's ruling People's Party, eager to oust his non-violent but still pro-independence Basque Nationalist Party (PNV) from office. And all without being master in his own house. Now, re-elected in May with an increased share of the vote, he has the chance to show his real worth.

Mr Ibarretxe's first problem, and far the greatest, is ETA. But his second is within his own party: its veteran leader, Xabier Arzalluz, a 68-year-old still in his heart fighting Francoist repression. It was Mr Arzalluz who cajoled ETA into a ceasefire in 1998, in return for a joint political offensive to win greater independence. When that got nowhere and ETA, after 14 months, called off its truce, it was Mr Ibarretxe who had to break his party's new-formed links with ETA's political wing, hold office without a majority and bolster morale in the regional police force as it faced renewed street violence and murder, all under a hail of insults from the government in Madrid, which treated his administration and ETA almost as two sides of one coin. And, by the way, he had to govern too, for the Basque region has even wider powers—in taxation, for instance—than do most in Spain.

Now, elected with nearly 43% of the vote and 33 seats in the 75-seat parliament, six more than in 1998, the PNV-headed alliance has to prove the voters right. Mr Ibarretxe has made a fair start. ETA, whose political wing took a battering in the election, showed its view of democracy by a murder in Madrid the night before he addressed the new session of the Basque parliament last week. Once again he had to begin an important speech remonstrating with the terrorists, his features twisted with genuine distress. But he went on in firm voice, celebrating what he described as "a feast day for Basque democracy"—and condemning ETA in the harshest terms used by any PNV leader since the truce broke down, a compliment that ETA returned with two murders on July 14th, the very day on which he was to swear his oath of office under the legendary oak tree of Guernica where Basque elders used to meet.

Still more strikingly, he promised to rebuild bridges with other political parties and to work with the central government in the fight against terrorism; and he set any moves towards Basque self-rule within the framework of existing institutions. That, in his eyes, could mean—for a start—more devolved powers. It could also mean (to him, though the centre does not think so) a constitutional change that would admit the now-unrecognised possibility of steps to independence.

This conciliatory tone was in striking contrast to Mr Arzalluz's sometimes irascible and always fiery language. It was typical of a man whose appeal lies in his integrity, capacity for hard work and attention to detail. It was those qualities that drew friends of his to suggest he should stand for office as mayor in his home town of Lloido soon after he had finished studying economics and business at a nearby public university.

There he had been considered a solid, methodical student, hardly the stuff of which nationalist politicians are made. Born in Alava, the least Basque of the region's three provinces, he was not a Basque-speaker, let alone a member of the PNV, though his family had nationalist sympathies. But once bitten by the political bug, Mr Ibarretxe joined the party and rose swiftly, moving to the provincial assembly where he caught the eye of PNV leaders including his predecessor as regional premier, Jose Antonio Ardanza, another cool and contemplative politician much unlike Mr Arzalluz. While Mr Ibarretxe struggled to learn the complex Basque language—a necessity for anyone with ambitions in the party—Mr Ardanza pulled

him into the government in 1995, made him his deputy and set him to handle complex financial negotiations with the central government.

He did it shrewdly. After a marathon session until well after midnight, Spain's finance minister suggested that the negotiators should get a few hours sleep, leaving the documents to be drawn up and signed thereafter. Mr Ibarretxe insisted on copying the deal by hand and signing it that night, lest the Catalan nationalists, whose aid the government needed in the central parliament, should learn the terms and demand the same for their region, prompting the government to backslide.

He will need this canny doggedness in his new dealings with the centre. Mr Ibarretxe has not abandoned the commitment to independence expressed by Mr Arzalluz in the approach to ETA's truce; but he has set limits, notably that any discussion of proposals for further autonomy will take place in the Basque parliament, and not, as in 1998, in an all-nationalist conclave. Spain's prime minister, Jose Maria Aznar, though still insisting that the fight against ETA comes first, has responded in a far mellower tone than had been heard for many months.

The road ahead?

Does that mean political progress? Mr Arzalluz seems to think so. He used to doubt Mr Ibarretxe's effectiveness, but now recognises that it was the calm style of the younger man (Mr Ibarretxe is 44) that won the PNV victory in May, and avers that he himself is ready at last to retire. That would open the way for fresh thinking in the PNV.

Socially, his ideas are further left than has been usual in the PNV, traditionally—in this respect—close to local big business. People, he insists "are more important than the market". But on the big issue, Basque independence? Like many politicians in Spain, Mr Ibarretxe is adept at twisting European notions to suit his needs. "We do not want to create an old-style nation-state," he says. "Subsidiarity and loss of sovereignty are familiar terms to us in the European context. Why make them taboo here?"

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Medical negligence

Tragic flaws

Jul 19th 2001
From The Economist print edition

How can doctors be made more accountable for their mistakes?

TO ERR is human, but getting medical professionals to own up to such frailty is far from easy. At Bristol Royal Infirmary, between 1984 and 1995, more than 90 babies were injured or died during open-heart surgery. The death rate for these procedures at Bristol was roughly twice that at other centres in Britain, but this did not deter surgeons and managers.

Eventually, the persistence of a "whistle-blowing" colleague and a certain number of stories in the press forced the hospital to admit its failings. The result was a public uproar. Two of the three physicians most embroiled in the mess were struck off the medical register. The Department of Health called for an independent inquiry to determine what went wrong, and what should be done in future to improve the quality of health care across the National Health Service (NHS).

On July 18th, three years and £14m later, the inquiry published its findings. Blame is largely reserved for medical and managerial culture, rather than for individuals. The report points to a failure, not just at Bristol but across the whole NHS, to recognise the importance of setting and enforcing standards of clinical practice. It shows up the dire consequences of not having a systematic approach for gauging the performance of practitioners and hospitals. It laments the lack of accountability to patients and their families, where the process of informed consent was seen by hospital surgeons as a tiresome chore rather than a right.

The "club culture" of the hospital, where senior doctors were above suspicion, is also criticised. Perhaps most disturbing is the fact that, by 1990, surgeons at Bristol had more than enough data to know that something was seriously wrong, but there was no clear chain of command to put a stop to it. Surgeons pressed on in the hope of getting better, but in retrospect this "learning curve" looks more like a slippery slope.

The inquiry makes almost 200 recommendations on how the system can do better in future and save some of the 25,000 lives that may be lost annually as a result of less spectacular medical errors, such as misprescribed drugs. These range from back-to-basics initiatives—retooling medical education, for instance, to ensure that future doctors are better team players—to building performance targets into all practitioners' contracts.

Certain reforms are already afoot. The General Medical Council, for example, which licenses doctors in Britain, is working on a "revalidation" programme that would assess physicians' competence every five years. The government is in the process of introducing best-practice guidelines for the treatment of various medical conditions. The inquiry recommends new responsibilities for agencies such as the National Institute for Clinical Excellence and the proposed National Patient Safety Agency, and better co-ordination between them, so that outcomes of medical treatment are methodically collected, analysed and acted upon to nip Bristol-like tragedies in the bud, if not prevent them all together.

Such reforms are laudable in principle, but they will bring problems in practice. For example, one recommendation is to make information about the performance of hospital and medical teams widely available to the public. But unless such data is carefully adjusted to account for important variations between groups, and presented in a user-friendly format, it is likely to bring more confusion than clarity to patients.

That said, appropriate information can be useful. A recent study from the Nuffield Trust, a policy group in London, shows that in America some high-quality information has, in some cases, improved the performance of hospitals, even though individual patients and physicians have had little use for it. But, as

Steven Dewar of the Kings' Fund, a health care policy group, points out, even if such information were available to British patients, the NHS gives them little latitude to act upon it. They do not get to choose which hospital will do their triple bypass. And without choice, information is not very useful.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Leadership election

The battle for the Tory party

Jul 19th 2001
From The Economist print edition

Who becomes the next Tory leader depends on which is stronger—the party's hatred of Europe or its survival instinct

Get article background

IF THE Conservative Party is about anything, it is about power. It has had more time in government than any other democratically elected party anywhere in the world. Yet the Tories, battered in two successive elections, are now heading for a bruising two-month leadership race between a right-wing Eurosceptic, Iain Duncan Smith, and a leftish pro-European, Ken Clarke. These men, whose names will go forward to the party membership after they topped the poll in the parliamentary party on July 17th, represent opposite ends of the party, not just on Europe but also on social issues.

Whoever wins, some will depart. The left-leaning vice-chairman of the party, Steven Norris, has indicated that he could well defect if Mr Duncan Smith becomes leader. A victory for Mr Clarke would be met with equal disgust by many of the party's right-wing anti-Europeans.

The exclusion of the early favourite, Michael Portillo, who got 53 votes—one less than Mr Duncan Smith and six fewer than Mr Clarke—came as a shock. Front-runners rarely win Tory leadership contests, but Mr Portillo, who put himself forward as a unity candidate, had the backing of nearly two-thirds of the shadow cabinet. His failure to secure one of the two places on the membership ballot is partly the result of a misjudged campaign and partly the consequence of ancient Tory prejudices (see article).

Mr Portillo's defeat robs the Tories of one of their most powerful figures. He has said he wants nothing more to do with front-bench politics and will look outside Parliament for employment. His supporters are stunned. Nicholas Soames, a former defence minister, said the result was a tragedy because "it will make flesh the polarisation that exists in the party." Raymond Mobiot, former president of the Conservative National Convention, rues the fact that there is no compromise candidate and that the membership is faced with such a stark choice.

Mr Clarke, former chancellor of the exchequer, home secretary and health secretary, is a formidable debater. His blokeish exterior belies a shrewd and adaptable politician who is on the left of his party. He has never been willing to compromise his pro-European views—they lost him the last leadership election—but he does not expect to impose them on his mostly Eurosceptic colleagues. In a blunt warning at a press conference on July 18th, he said, "We wrecked the party in the past ten years on Europe, and headbangers on either side will wreck it again if we let them."

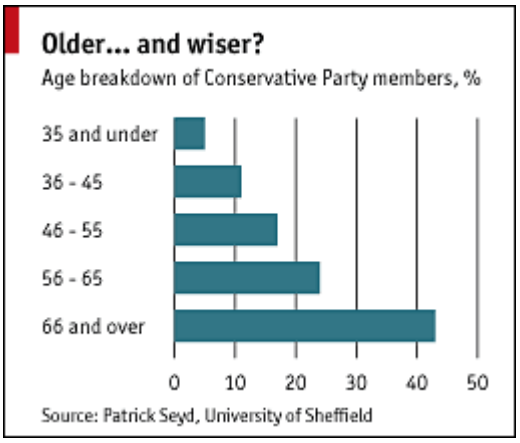
Mr Clarke will struggle to convince traditional Tories that they should back him despite his views on Europe. But he has some strong cards to play. He came top of the parliamentary poll and at least half his support came from MPs who do not share his pro-European views—which suggests that his personal appeal transcends that of his views. For a Tory, he is popular in the country: according to an ICM poll, 4% of people would be more likely to vote Conservative if he were elected leader.

Mr Duncan Smith, who served as a captain in the Scots Guards, is an uninspiring speaker, has no government experience and is described by his critics as "William Hague without the jokes". But his Euroscepticism and right-wing views on social issues such as hanging and homosexuality are close to

those of the party's grassroots. The Tory papers, notably the *Daily Telegraph*, the *Daily Mail* and the *Sun*, which helped destroy Michael Portillo's candidacy, will back him. Lady Thatcher is also likely to come out publicly in his support. Voters are less impressed. The ICM poll found that, if Mr Duncan Smith were leader, 8% of people would be less likely to vote Conservative.

The party members who will choose between them are, by virtue of their age (see chart), unrepresentative of voters as a whole. Two-thirds of them are either retired or near retirement. Patrick Seyd, professor of politics at the University of Sheffield, who did the last comprehensive survey of the membership, believes that it could now have fallen as low as 230,000. It has almost certainly not got any younger, he says.

The age profile of the party could determine the result of the election. Conversation with party members suggests that Ken Clarke's strongest constituency is among younger urban members. Paul Bristow, deputy chairman of Conservative Future, the organisation for young Conservatives, says that for the Tories to prosper they have to appeal to first-time voters and young people who have not voted before. Yet most Conservative members, according to the Tory agent in Hammersmith and Fulham, will be voting for the candidate "whose views most accord to their own".



This is the first Conservative leadership election in which party members have had a say. Democracy has come late to the Tories. Whether it does them any good will depend on whether they are able to bury their ancient prejudices and remember what it is that the Tory party has excelled at in the past: winning power.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Tory homophobia

To fall like Lucifer

Jul 19th 2001
From The Economist print edition

The Tories embrace economic change. Social change is more of a problem

Get article background

BY THE standards of modern Britain, Michael Portillo is a fairly normal person. His political views have changed, and he is open about it. He is the son of an immigrant. And, although he is now married, he admits to having had homosexual experiences in the past. By the standards of the Conservative Party, however, that makes him unusual—unpalatably so.

Homosexuality has been legal in Britain since 1967, but many Conservatives still could not bring themselves to support a leadership candidate who had openly admitted to a gay past. This is especially true of the older members. One former naval officer in a true-blue Tory seat put it quite succinctly: "I just can't stand bloody poofters." Others will talk more euphemistically about the subject. As one constituency chairman argues, "letting it all hang out does not go down well with some of our activists." And the MPs who rejected Mr Portillo have spent a good deal of the last three weeks listening to their activists.

Mr Portillo's chances of winning were compromised right at the start of the campaign when Lord Tebbit, the pin-up of the right-wingers, compared childless Mr Portillo to the "normal" Iain Duncan Smith. Never mind that Mrs Portillo had medical problems that made her unable to have children. The coded message struck a chord with many of the faithful who put great store by the party's reputation as the guardian of "family values". Some activists lament the fact that, at the recent general election, none of their three main spokesmen—William Hague, Mr Portillo and Ann Widdecombe—could parade any children in front of the cameras.

Whereas Labour has had openly gay ministers, such as Nick Brown, minister of works and pensions, the Conservative Party has remained largely in the closet. Only one Tory has ever admitted to being a homosexual while serving as an MP. Very occasionally an MP has been found out and has had to resign. Ian Harvey was caught with a Guardsman in St James's Park in 1958. He entitled his memoirs "To Fall Like Lucifer".

Everybody knows that there have been many homosexual Tory MPs: Mr Portillo's crime was to speak openly about it, or even to "make an issue" of it. John Barnes, a historian of the Conservative Party at the London School of Economics, argues that although there has been plenty of homosexuality among Tory MPs, "the party has never had it thrown in their face before." Torche, an organisation for homosexual Tories that campaigns for equality and openness within the party, can count prominent personalities among its ranks, such as David Starkey, a historian, but no MPs.

Hywel Williams, a homosexual former Conservative cabinet adviser, argues that the party's attitude towards homosexuality is part of a wider set of fears, "of the modern world and of change in general". So Mr Portillo's defeat has exposed the paradox at the heart of Conservatism: the party that has most willingly embraced economic change most strongly resists the social change that inevitably follows.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Nightlife

Old school tie

Jul 19th 2001
From The Economist print edition

Chains of late-night bars and clubs are spreading around the country

The branded experience

THE 29-year-old information-technology consultant was clear about why she was dressed in school uniform. “Men in shorts,” she said. “That’s why we’re all here.” Thus, perhaps, the extraordinary popularity of SchoolDisco, where 2,000 twenty-somethings come week after week, wearing uniform and old school ties, to dance to dated music and drink alcopops. But there is something odd on the ceiling: Moroccan awnings. This is a nightclub that wants to be a Bedouin tent. It was once the Hammersmith Palais, in West London, until it was bought by a chain of late-night bars with a North African flavour called Po Na Na. Exploiting the craze for mock school discos is its latest move.

Late-night drinking is changing. In a field dominated by individual owner-operators, larger chain bars are growing quickly. In 1995 Po Na Na had one bar; now it has 29 around the country, largely in student towns. Drapes, lamps, cushions and furnishings are imported from Marrakech, and in all of them the theme is tongue-in-cheek Middle Eastern. Po Na Na owns nightclubs, but its bars are more relaxed affairs without the focus on loud music and dancing. Drinks are served until 2am, a big attraction in Britain’s unreformed licensing regime.

The upside to branding venues is the usual one—familiarity and reassurance. But there is a downside, too, admits Christian Arden, who has run Po Na Na from its inception. “People hate paying lip service to a corporate roll-out,” he says. His solution is to give individual area managers control of their own advertising, entertainments, pricing, door policy and so on. “Our managers have to know what it takes to make their place the cool, chic place in town,” he says. “We haven’t got egos about what we say goes. If we suggest something and it’s challenged: absolutely fantastic.”

Not everyone is as nervous about branding nightlife. Stephen Thomas heads Luminar, Britain’s largest conglomerate of bars and clubs. He runs a string of branded venues, each targeted at different niches of the population, and can’t see anything wrong with this approach. “I’ve never met anybody who says they refuse to go into our bar because we’ve got 59 others,” he says. “Nobody cares in Bristol what’s going on in Basingstoke. It would be completely bizarre to think that’s a logical thought process.”

Chain bars make good business sense: they have greater buying power, can deal with licensing authorities more easily and can offer staff better career opportunities. The difficulty for Po Na Na is staying trendy despite its size. It hasn’t done badly so far, but it isn’t easy. And playing the youth market can lead a company down some surprising avenues. Back in the school disco, a man from Essex in a gown and mortarboard is energetically thwacking strangers with a cane. “Can you think of anything better?” he asks. Indeed not.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Gambling

Paris, Nevada; Luxor, Lancashire

Jul 19th 2001
From The Economist print edition

Blackpool plans to reinvent itself as a glamorous casino venue. Pigs may fly

LAS VEGAS, Nevada, likes to claim that it contains nine of the world's ten largest hotels. To say nothing of Paris, Venice, New York and the Pyramids, which are also in town. The average summer temperature is 41°C, and some 30m people visit the city every year.

Now Blackpool, Lancashire, wants a piece of the action. It may not be able to compete on temperature (average in summer 19°C), but the run-down resort hopes that it may be able to re-invent itself as another capital of gambling.

Such dreams have been encouraged this week by the Gaming Review Body's report on the future of Britain's gaming laws. Commissioned by the government and chaired by a former Treasury adviser, Sir Alan Budd, the report recommends a radical liberalisation of the country's restrictive gaming laws, paving the way for casino hotels with no limits on payouts and none of the silly current restrictions that force casinos to become clubs, and new members to wait 24 hours before they can play.

The recommendations are unlikely to become law for several years. But they have met with a sympathetic response from the government, despite those opponents of deregulation who worry that the nation's current total of 400,000 gambling addicts—a number frequently bandied about by the disapproving—will lapse further into sin.

Blackpool, anyway, is delighted. Leisure Parcs, which has recently bought up most of Blackpool's most famous landmarks, wants to build Pharaoh's Palace, a riot of Luxor-style Egyptiana to rival the Pyramids (the ones in Nevada, anyway). Quite why ancient Egypt has become synonymous with gambling has never been explained, but this particular palace will have 1,000 bedrooms, a theatre, 80 gaming tables and 2,500 jackpot machines. Five similar hotels are also planned to replace the tacky, clapped-out frontage that currently passes for the town's sea-front "Golden Mile".

These plans represent a quantum leap both for the country's gaming industry and for its seaside resorts. But are they realistic? Las Vegas made it big because Nevada's gaming laws were more liberal than those elsewhere in America. Blackpool will be playing on an uncomfortably level playing field. And the town has a long way to go to rebuild its old reputation for fun. Even the Labour Party has decided that it is too depressing a venue for its annual conferences.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Transport strategy

Going nowhere

Jul 19th 2001
From The Economist print edition

Without more money, the government's transport strategy will fail. That's the view not of a protest group, but of the head of the Strategic Rail Authority

THIS week the row about London's underground boiled over again. The prime minister sacked Robert Kiley, transport adviser to Ken Livingstone, London's mayor, as chairman of London Transport. Mr Kiley's failure to reach an agreement with the private-sector bidders for the tube, combined with the mayor's legal challenge to the government's private-public partnership (PPP) plans, had made his position untenable.

But sacking Mr Kiley solves nothing. He remains Mr Livingstone's transport supremo. The government remains committed to handing over the tube to Mr Livingstone under the PPP. Mr Livingstone and Mr Kiley remain implacably opposed to the PPP. The affair goes to the courts next week.

The row over the tube is good drama, but the government's wider difficulties over its transport strategy are arguably more important. A measure of the scale of the problems was the decision this week by Stephen Byers, the new secretary of state for the Department of Transport, Local Government and the Regions (DLTR), to grant two-year extensions to the current passenger-train operators. This in effect reverses the strategy of the Strategic Rail Authority (SRA) of giving 20-year franchises in return for commitments to invest in new trains and better services.

Mr Byers had little choice. The current chaos and the need to redefine Railtrack's role make it almost impossible to reach long-term franchise agreements. So far, out of a total of 25, only three franchises—for Chiltern Railways, South Central and South West Trains—have been agreed. The train-operating companies are understandably furious as their targets of increasing passenger numbers by 50% and freight by 80% by 2010 are looking ever more distant.

Delaying franchise renewal is bound to delay much-needed investment. The claim that more than half of the £60 billion planned investment in rail will be provided by private capital now looks hopelessly

unrealistic. Railtrack was supposed to have provided £8 billion for new track and infrastructure developments. But the company is in such a weakened state that it is not in any position to raise new money from its shareholders.

Rail finance is under acute strain because the rail regulator has reduced access charges paid by the train-operating and freight companies. The effect is to reduce the funds available to the SRA for investment. Another blow to the railway's finances is the expensive safety recommendation made by Lord Cullen's inquiry into the Paddington rail crash. This requires Railtrack to fit the advanced train-protection warning system, a fail-safe method of stopping trains in danger, which will cost more than £2 billion.

It is now clear that most of the money for investing in the rail network will have to come from the government. But the Treasury is not willing to agree to anything until it has a better measure of the final bill. Relations between Sir Alastair Morton, the head of the SRA, and ministers have reached the point where he is threatening to resign, and the government seems happy to see him on his way. He is due to leave his post next year but advertisements for his replacement have already been published. Sir Alastair has warned ministers that, without a lot more government money, the ten-year transport plan is doomed to fail.

It is not only the railways that are in trouble. The government wants to reduce congestion on the roads by 6%; but the government-financed Commission for Integrated Transport, which is reviewing the progress of the ten-year plan, doubts that the target can be met. The commission has pointed out that current price signals are tilted in favour of the use of cars and heavy vehicles. Its chairman, David Begg, wants to explore whether road pricing could replace vehicle excise duty and petrol duties.

Phil Goodwin, head of the Centre for Transport Studies and an adviser to the government, shares the commission's scepticism about congestion targets. His study, "Running to Stand Still", points out that the £60 billion planned investment in the road network will do little to reduce congestion. For most drivers, the time-savings, about a minute on a 60-mile journey, will be so small as to be invisible.

The government has fallen into the same trap as it did with the National Health Service: it is promising more than it can deliver. Sir Alastair argues that significant improvements on the railways are probably 15 years away. On the roads, congestion is almost certain to get worse (unless an economic slowdown curbs it) until nationwide road pricing is introduced. The job of transport minister has never been a route to political fortune. Mr Byers has learnt quickly that he has drawn the shortest of ministerial straws.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com WORLD BRITAIN
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Bagehot

Robin Cook's revenge

Jul 19th 2001
From The Economist print edition

The former foreign secretary may at last have found a cause worthy of his ambition

IF YOU own a poodle, you will not be fatally savaged by it. But even a poodle can give you a nip. And when it does, you have no way of knowing what is going on inside its pomaded head. You are mildly annoyed; it thinks it has struck a blow for freedom. For all you know, it is under the illusion that it has permanently reversed the (im)balance of power between you. It may try to take you for a walk tomorrow morning.

In the House of Commons, the back-bench Labour MPs who have been denigrated so often as Tony Blair's poodles decided this week to give the prime minister a nasty nip. They voted to reinstate two colleagues, Donald Anderson and Gwyneth Dunwoody, whom government whips had tried to remove as chairmen of two House of Commons select committees. Mr Blair no doubt finds this public reversal annoying—more annoying, certainly, than Mr Anderson and Mrs Dunwoody ever were as the occasionally troublesome chairmen of, respectively, the foreign-affairs and transport committees. Just when Mr Blair was beginning to live down his reputation as a "control freak", the label is back, and in the very week that he sacked Robert Kiley, the popular American who as chairman of London Transport had had the temerity to obstruct Mr Blair's impenetrable plan to revive the capital's Tube by means of a "public-private partnership". Hilary Armstrong, Mr Blair's new chief whip, whose job is to calculate how much humiliation his MPs are willing to put up with, got her first big guess calamitously wrong. Frank Field, a talented former minister who was also cast off a select committee but not reinstated, warned the government against creating the impression of riding roughshod over all its critics. When difficult times came, he said, "the electorate will have marked our card indelibly, and retribution will be visited upon us".

Portentous stuff. But to judge by their continuing excitement two days later, some of the MPs who voted to restore the two wronged chairmen are in danger of letting a modest victory go to their heads. One idea going around likens the little rebellion to John Dunning's famous resolution of 1780—the one in which Parliament complained of George III that "the influence of the crown has increased, is increasing, and ought to be diminished."

Under Labour, the power of the prime minister has increased, is increasing and ought to be diminished. But this week needs to be kept in perspective. Though Mrs Armstrong guessed wrong when she guessed that Labour MPs would swallow the removal of the two chairmen, she was doing nothing new. The parties' whips captured the select committees long ago: in 1992, John Major's Conservative government removed Nicholas Winterton, the (Conservative) chairman of the health committee, who had become a thorn in Mr Major's side. Moreover, as thorns go, neither Mr Anderson, who is decent, nor Mrs Dunwoody, who is indomitable, is actually quite as sharp as it now suits their defenders to pretend. Their sacking looked spiteful, and by reversing it the legislature has probably done something to keep the executive honest. But their reinstatement will not itself make the government's life very much harder. Even the sharpest of chairmen have struggled to give these committees teeth. They have the power to cause embarrassment, little else.

Crime and non-punishment

A cur that turns on its master is liable to bare its fangs again. Conventional wisdom said this week that, having broken the spell of the whips, Labour's newly unafraid backbenchers would henceforth give the prime minister a harder time. The trouble with this idea, says Philip Cowley, a political scientist at Hull University, is that seven out of ten of the Labour MPs who voted to reinstate the sacked chairmen had already voted against the government at least once in the previous parliament, and on whipped votes,

not a semi-free one of the sort held this week. Mr Blair's backbenchers were never quite the poodles of lore. They have grown nippier over time: there were more rebellions in the third session of the last parliament than in the first two put together. But this was for the familiar reasons—declining fear of the opposition, growing self-confidence, a swelling number who have lost hope of promotion—not because Mr Blair has abused Parliament's prerogatives in some novel way. The theory that this rebellion changes everything does not hold up.

Except, perhaps, in one way. A Conservative MP, Sir George Young, said that this week that the leader of the House, a cabinet minister responsible for getting the government's business through, should not also be the chairman of the Commons "modernisation" committee, which tries to strengthen Parliament's ability to hold the government to account. Normally, Sir George would be right: there is an obvious conflict between the two jobs, which is why Margaret Beckett, leader of the House in the last parliament, did so little to strengthen MPs' powers. After last month's general election, however, Mr Blair plucked Robin Cook cruelly out of the job he loved as foreign secretary and made him leader of the House in Mrs Beckett's place.

The prime minister may come to regret this. Mr Cook did not welcome demotion. He is said to have thought hard before accepting his diminished role. But that was before the Commons became suddenly interesting. Whereas Mrs Beckett would have fumed and snorted during the select-committee rebellion, Mr Cook put himself smartly on the backbenchers' side. He spent this week making all the noises that she would not have made about strengthening the committees' role: perhaps by relaxing the grip of the whips, perhaps by paying their chairmen extra, perhaps by debating their reports as a matter of course in the Commons chamber. Though it would not be fair to accuse Mr Cook of finding in his new job an unlooked-for opportunity for revenge against the man who demoted him, he may want to end his career with an Indian summer, as a parliamentary reformer. That should give any control freak something to worry about.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Lord Archer

A taste for fiction

Jul 19th 2001
From The Economist print edition

How did Lord Archer get away with it for so long? Powerful friends, draconian libel laws and a supportive wife

Going down

LADY ARCHER once spoke of her husband's unusual talent for embroidering the facts. "Jeffrey has a gift for inaccurate précis," she said. This week real life finally caught up with the former deputy chairman of the Conservative Party and candidate for London's mayor when he was sentenced to four years' imprisonment.

The charges of perjury and conspiracy to pervert the course of justice on which the millionaire novelist-cum-politician was convicted at the Central Criminal Court stem from his successful libel action 14 years ago against the *Daily Star*. The newspaper had alleged he had lied about his relationship with a prostitute, Monica Coghlan, and was forced to pay him a record £500,000 ($800,000) in damages.

The fact that Lord Archer lied throughout his libel trial was widely suspected at the time. It was common knowledge among his personal staff that his alibi was bogus and that the diaries on which he based his case had been concocted. This was not his first brush with dishonesty. He had lied about his academic record, fiddled his expenses as an official of the United Nations Association, been caught shoplifting in Canada and improperly dealt in shares in a company of which his wife was a director. All this was documented in Michael Crick's biography of Lord Archer, first published more than six years ago.

The mystery is not that the truth has finally emerged but that it has taken so long to do so. How was this obvious charlatan able to pursue a political career for so long? For three reasons: powerful contacts, the libel laws and Lady Archer.

Lord Archer put politicians and journalists in his debt by showering them with favours, flattery and hospitality. Thirty years of assiduously campaigning for the Conservative Party and courting its leading figures paid off handsomely. Lady Thatcher first nominated him for a peerage. When that was turned down, her successor, John Major, put him up again. Both backed his candidacy for mayor of London. Eight former senior Tory cabinet ministers—Norman Lamont, Michael Howard, Cecil Parkinson, Malcolm Rifkind, Brian Mawhinney, Peter Lilley, Tom King and Norman Fowler—also publicly supported him. In a letter to the *Daily Telegraph*, they declared he had "the vision, energy and commitment to be an outstanding mayor". William Hague, who as Conservative leader accepted Lord Archer's invitation to train in his gym, gave him his backing as "a man of honour and integrity".

Such influential friends undoubtedly had a chilling effect on journalists tempted to look into his affairs. So did the libel laws. Britain's are the most draconian in the world, even after recent reforms. Many papers had damaging material in their files about Lord Archer which they were scared to run because he was rich, powerful and litigious. The huge amount he had won against the *Daily Star* and the *News of the World*, which, together with costs, totalled more than £1m, terrified editors and newspaper lawyers.

Lastly, Lord Archer had his wife Mary to thank for the protection she gave him. Famously described as "fragrant" by the judge in the libel trial, her tearful claim that "we have a very happy marriage" undoubtedly helped Lord Archer win his action. Her continued support, despite his known philandering, was invaluable to her beleaguered husband's public career. Speaking to the judge in his libel trial, Lord Archer acknowledged the amount he owed to his wife: "I say this without reservation. Mary was the most

remarkable woman I knew when I was young and she remains that way now, sir."

Maybe the moral of Lord Archer's career is that you get found out in the end. Or maybe it is that favours can be bought quite cheaply in British public life.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Putin's choice

Jul 19th 2001

Is Russia under President Putin heading for regeneration, stagnation or decay? Probably all three at once, says Edward Lucas

AP

FROM the outside, it looks pretty good. For more than a decade, Russia has been, more or less, a democracy and a market economy, and on civilised terms with its neighbours. Against the dismal standards of Russian history, that is a big achievement. But so far the fruits have been meagre, bringing little comfort to most Russians. All they can see around them is physical, cultural and moral decay.

The paradox is underpinned by three contradictory trends at work in today's Russia. The first is revival. This started under Mikhail Gorbachev, as the Communist monopoly of power and the planned economy collapsed together. That allowed the beginnings of independent life in many spheres. Freed from totalitarian controls, the energy and brains of millions have brought countless changes for the better. There are plenty of new businesses, and such old ones as have survived are better run than they used to be. There is room for public-spiritedness and do-gooders. The crippling fear of the gulag is gradually being eroded by time. And Russians have started travelling. Instead of being isolated and bombarded with propaganda, millions every year see other countries with their own eyes. That has already begun to change their view of the world. And for many of those who cannot travel, at least ideas from all over the globe are only a mouse-click away.

The second trend, though, is stagnation. The collapse of communism, it turns out, was superficial and partial. Well-connected people and organisations—especially the security services—started clawing back power straight away, and many became rich as well as powerful. Changes for the better are often stopped in their tracks by greedy bureaucrats, and by the peculiar difficulties and perversities of life in Russia. The state, at all levels, dislikes criticism and opposition. Many Russians, for their part, still hanker for the certainties, real or imagined, of the past: tradition, authority and unity, rather than experiment, competition and pluralism.

The third trend is accelerating decline. Nobody in Russia's political or economic elite has seriously tried to halt the downward slide that underlay the Soviet Union's defeat in the cold war. Most of what the Soviet Union built was shoddy to start with, but modern Russia lacks the money and willpower to sustain even that unimpressive standard. As a result, the country is falling apart. Things built during the Soviet era are crumbling, leaking, rusting and rotting. Spills, collapses and fires that in other countries would cause a huge public outcry are shrugged off as everyday events. The education system is being corroded by low

salaries and corruption. Worst of all, Russians are simply dying out: smoke-ridden, drink-soused lifestyles, together with unchecked infectious diseases, have created a demographic abyss. According to one gloomy prediction, the population could fall from 145m now to 55m by 2075.

At first these three big shifts were masked by the wild optimism, savage pessimism and sheer upheaval following the collapse of the Soviet Union. In 1993, Russia flirted with civil war when the president of the day, Boris Yeltsin, turned heavy artillery on the parliament building. For much of the 1990s, political extremism seemed a real threat: in the 1993 parliamentary election, the ultra-right party of Vladimir Zhirinovsky won a quarter of the votes. Mr Yeltsin beat his Communist rival, Gennady Zyuganov, in the 1996 presidential election partly by rigging it. Oligarchs (politically influential tycoons) strutted the stage, apparently more important than politicians or officials. In the provinces, local chieftains ignored the centre and declared their tinpot republics “sovereign”. Organised crime became a feature of everyday life.

Pride before the fall

On the economic front, the early 1990s brought hyperinflation and food panics. But there were also high hopes, fuelled by the thought of vast quantities of underused brainpower and raw materials that were now joining the world economy. Some talked of a coming boom that might take Russia's income per head above Spain's by 2010. Such wishful thinking led to the financial bubble of 1997-98, when hot money from abroad piled into flimsy stocks and bonds, culminating in the default, devaluation and banking collapse of August 1998. This was followed a year later by a big money-laundering scandal. Russia turned from darling to pariah.

In the main, both the fears and the hopes have now receded. Life may not be much better, but at least it has become a lot calmer. Indeed, by past standards Russian politics and economics are now quite dull. Most people who matter agree about the economic and political direction the country has to take: it must embrace markets, private property, a stable, convertible currency, regular elections and freedom to travel abroad. Where once the Duma—the lower house of parliament—furiously tried to impeach the president, and the Kremlin sacked prime ministers on a whim, the worries now are about missed growth and inflation targets or the slow progress of useful bits of legislation.

That is not to say that everything in Russia's garden is lovely. Poisonous patches include the costly and debilitating war in Chechnya; officialdom's contempt for outsiders, especially weak and poor ones; corruption; the ill-treatment of minorities; and blindness towards the past. But however skewed and unfair the rules are today, at least they are not changing continually and unpredictably. Stability is a huge plus. Today's Russians, who have endured enough change to last them several lifetimes, certainly value the current calm. They also prize Vladimir Putin, the president whom they see as its architect.

If the present seems just about tolerable, though, there are big question marks about the future. Is the recent political and economic solidity just a temporary lull, after which Russia's unsolved problems will crowd forward again, bringing new disasters in their wake? Or will Russia muddle along like this for years—economically stagnant, politically not as democratic as many might wish, a pretty miserable place to live for most of its people, but at least a menace neither to itself nor its neighbours? Or might this new stability—just possibly—serve as the base for the profound changes needed if Russia is to become a full member of the developed and democratic world, as its size, its culture and its past achievements suggest it should? These are the questions this survey will explore, starting with the simplest and crudest gauge of success: the prospects for sustainable economic growth.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Good in part

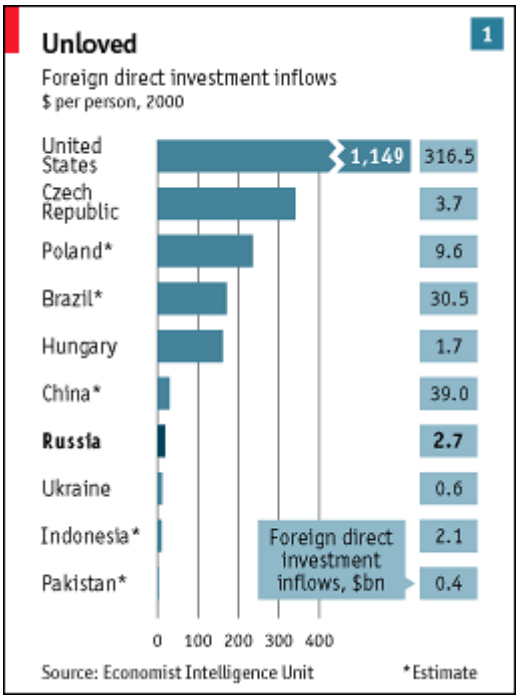
Jul 19th 2001

The economy has picked up, but foreign businesses are largely staying out of Russia

FOR the first time since the collapse of communism, Russia has a balanced budget, a thumping trade surplus, bulging reserves and a growing economy. This is heartening by past standards, but set against what needs to be done, it is still only a modest success, achieved in unusually helpful conditions. To reach the level of prosperity that even one of the poorer members of the European Union, such as Portugal (which Mr Putin has singled out for comparison), enjoys today, on a crude calculation Russia would need to grow by 8% a year for the next 15 years.

That looks very ambitious. Thanks to a big devaluation and a high oil price, the economy last year did grow by a spanking 8%, but that boomlet is fizzling out already. This year's growth will be more like 4%. At that rate, it might take Russia 40 years to reach Mr Putin's modest goal. Thanks to the money sloshing in from raw-materials exports, inflation is far too high—currently nearly double the 14% target the government has set itself for the end of the year, threatening to make Russian industry uncompetitive again.

According to Mr Putin's bearish economic adviser, Andrei Illarionov, Russia is suffering the early stages of the "Dutch disease" experienced by the Netherlands during the natural-gas boom there in the 1970s. Easy money from natural resources is keeping the exchange rate high and inflation up, and beginning to strangle the rest of the economy.



For the moment, though, land, labour and most other business costs still seem remarkably low in Russia. It might seem odd, then, that there is so little interest from outside. A vivid example comes from the depressed and depressing small border town of Ivangorod in north-western Russia. Across the river, in what in Soviet days used to be another part of the same town, very similar people—also ethnic Russians, but living in now-independent Estonia—earn up to $500 a month in thriving manufacturing enterprises. In Ivangorod, by contrast, industry has shut down almost completely, even at average wages of only $50 a month. In other parts of Eastern Europe, capital quickly moves across borders in search of cheap labour. Not here.

Even the best macroeconomic management will make little difference to that. It is not the marginal effect of a rising real exchange rate, but Russia's bureaucracy, along with taxes and bad management, that really holds back growth. So the main question is not whether the government and central bank can manage the country's finances sensibly, but whether Russia can become a long-term home to successful, competitive companies.

In the 1990s, that looked a long way off. Many managers were busy stealing cash from their businesses. Outside investors were there to be cheated. Business basics such as contracts, proper book-keeping and customer satisfaction were widely ignored. Barter was rampant. To make serious money, you dealt in raw materials or exploited political connections.

This has changed sharply. Most Russian companies are better—or at least less badly—run than at any time in living memory. Having feathered their personal nests, managers are now giving more thought to the longer term. Cash has replaced barter. Guns are no longer carried to board meetings. Company bosses worry about weaknesses in previously neglected disciplines such as

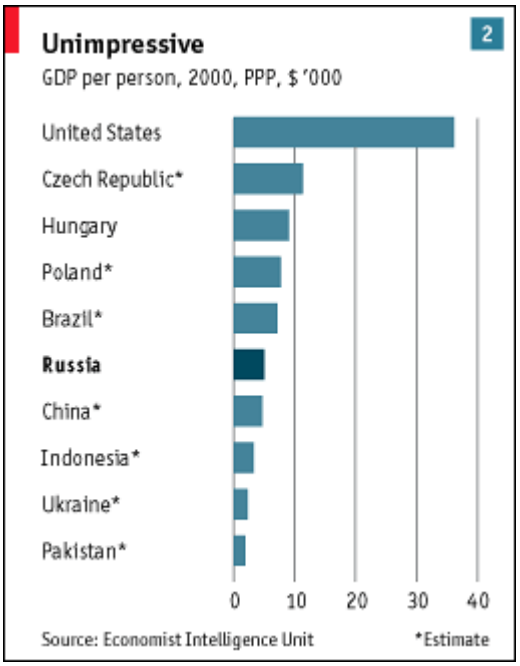
Most Russian companies are better—or at least less badly—run

finance and marketing. Most big companies publish accounts drawn up on the western model.

than at any time in living memory

So now rich firms are buying poor ones, and pepping up the management. Local producers of cheap, smartly packaged soap, chocolate and other goods are offering stiff competition to the multinationals. Some publicly traded companies, such as Yukos, an oil giant, have already enjoyed the spectacular effects that even a semblance of good behaviour can have on share prices. Yukos used to treat its shareholders like dirt, but since 1999 it has paid out $300m in dividends and spent perhaps another $50m on advertising and glad-handing. Its market capitalisation has shot up from $600m to $6.8 billion. The founder, Mikhail Khodorkovsky, is now a paper billionaire. If the company can eventually sell out to an international investor, he will become even richer.

But most Russian managers are nowhere near reaching international standards. They flourish only in a protected home market, helped along by political connections. Russian industry is subsidised by artificially low energy prices to the tune of at least $25 billion a year. There is no sign that a proper banking system is taking shape. Capital flight—which is still averaging at least $1.5 billion a month—shows that there is plenty of money. What is missing is opportunities.



For a snapshot of the problem, join the queue to see Viktor Bibikov, a powerful businessman and politician in the western provincial capital of Pskov. A dozen people are already waiting in his reception area, hoping to catch a word with the boss. A radio plays loudly in the background, over the crackle of his security men's walkie-talkies, while two secretaries field a deskful of telephones that ring constantly. A beefy colonel in the uniform of Russia's border guards barges past the queue and marches into the inner sanctum. After 20 minutes he emerges, chortling, barks some instructions down a telephone and marches out.

An hour later Mr Bibikov appears. He feigns surprise at the number of supplicants—most of whose appointments are now running an hour or two late—and genially invites everyone into his private office at once to sort out their problems simultaneously. This is crude but effective: nobody likes to discuss business in front of strangers, least of all when it involves favours and special pleading. A series of hurried conversations takes place, nervously whispered on one side, barked on the other. “I am not going to sign this,” snarls Mr Bibikov, tossing aside some papers involving a transport deal. “Go away and do it properly.” When he eventually settles down to talk about his businesses—a rich mixture of berries, cables, canned fish and freight—he is interrupted by numerous phone calls.

A bit of a scrum around the boss is a familiar scene, especially in third-world countries. But in Russia the habits it reflects are a big barrier to growth. Life at the top is about hierarchy, connections, influence-peddling and crisis management, not about organisation, forethought and planning. Mr Bibikov is forceful, cunning, well connected and perhaps lucky. His methods may seem odd to an outsider, but they have made him hugely successful by local standards. However, it is hard to see businesses run like this doing well in tougher and more transparent markets.

Life at the top is about hierarchy, connections, influence-peddling and crisis management

Seeing the wood for the trees

At first sight, Syktyvkar Forest Enterprise, in the remote middle of northern Russia, looks as much of a shambles as Mr Bibikov's time management. Roads are pitted, verges littered with derelict machinery, façades decayed. Inside, amid the deafening noises of logs being chopped, chipped and pulped, bent and slippery metal catwalks snake past lethal-looking machinery.

The headquarters building looks shabby too, but the new managers are as bright as buttons. They have spun off peripheral companies, slimmed the workforce and installed new technology. Where it matters, working practices have been transformed:

typewriters and carbon paper have given way to the most modern management software bought from Germany's SAP.

Plenty of trees, but where is the management?

A Russian-born, American-educated director, Stan Shulman, recalls how orders used to be handled:

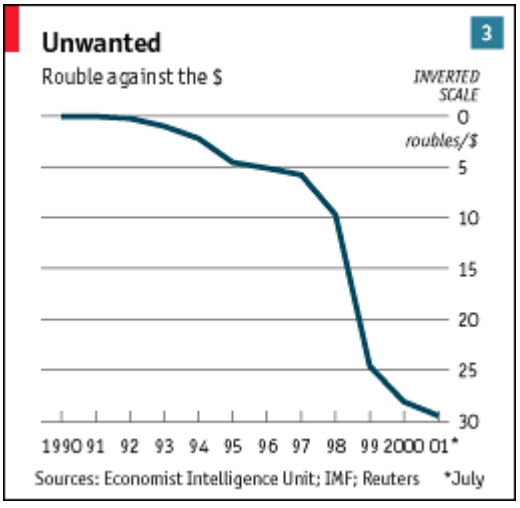
> Someone would come here and sit in line, and my predecessor would write a piece of paper, and it would go to another department with another file and other bits of paper, and the guy would wait months and months, and nobody knew exactly what he needed, and his order would go to a warehouse, and nobody would know where it was. Nowadays a salesman with a laptop sends the order via the Internet. The system checks the customer, then it goes straight into the production schedule, and we can tell the guy immediately when his order will be ready for shipping.

Basic stuff by rich-country standards, but still rare in Russia, because it takes a huge effort to make it happen. At Syktyvkar, everything had to change, from the way it paid its people to the buying of its logs. And all the changes had to be put in writing. Mr Shulman produces a 1,000-page tome outlining every detail of the new regime.

“Russian industry is now able to restructure: the age of stealing is over; the age of arrogance is over; the age of instability is over. But western thinking and know-how are still crucial,” says Mr Shulman. “You need someone on the inside who, for at least a certain period of time, checks, controls and helps. You have to teach Russian management to think in western ways, and also to understand that if you sign something, you have to do it.”

Paper is just the sort of business that Russia should excel at. It has plenty of trees; water, energy and labour are cheap; environmental standards (in practice, if not in theory) are undemanding. The missing ingredient is usually good management. Syktyvkar's shareholders decided in the mid-1990s to make the company efficient. After spending $175m on modernisation, it is now one of the most profitable plants in Europe, making profits of $80m on sales of $300m last year, half of them abroad. Its foreign investors receive accounts drawn up on the American model. Workers are paid well by Russian standards, although the value of their shares has been sharply cut by a complicated management ruse.

Syktyvkar's example shows how old Soviet companies can be turned round, given the will. But what of the new ones? Vested Development is a software company specialising in complex programmes for American customers. Although the biggest block of shareholders and most of the workforce are Russian, its headquarters, as well as most of its top management, is American.



This is partly to keep its customers happy. The more telling American contribution, though, is management skills. Russians are brilliant at geeky jobs, but less good at soothing nervous clients, patiently sitting through meandering brainstorming sessions, planning ahead and presenting their work slickly. Finding people to manage them is hard, too. “I can hire another 20 PhDs in mathematics tomorrow. I cannot find people with two-year-old MBAs wanting to be middle managers,” complains Brian Phelps, the company's boss.

Time and good salaries should eventually solve that problem. Russia is beginning to produce its own MBAs, although standards vary a lot. Many companies are training their own managers. But to become truly competitive, Russian firms seem to need a strong shove from outside, sometimes from a visionary local boss, more typically from a foreign owner.

Just buying in outsiders, as Russian companies are increasingly doing, does not usually do the trick: they do not have the clout to push through unpopular changes. One westerner who has advised some of Russia's top boardrooms describes them as “black boxes” because of their impenetrable networks. Most of them will take years to change.

If in doubt, lubricate

But it is not just lack of effective modern management that is holding back Russian business. Many companies also find that the country is still an awesomely costly place in which to do business. Bureaucrats gobble up both money and time. When Mr Shulman wanted to open a sales office in Ukraine, for example, he had to submit a business plan to the Russian Central Bank, approved by the Ministry of Finance, so he could transfer the $30,000 needed to open it. A bribe-seeking bureaucrat denied permission. For a big company such as Syktyvkar, that sort of thing is annoying but surmountable. “Look at bureaucracy as a cost of your investment and calculate your payback based on that cost, and you'll be all right,” says Mr Shulman breezily. And be flexible, he might have added. He solved the Ukrainian problem by finding a friend there to open an office with no formal ownership ties to Syktyvkar.

For smaller companies, though, such snags can be fatal. In Russia's Black Sea oil port of Novorossisk, for example, a local British businessman, Clive Rumens, wanted to set up a small factory producing a simple additive that makes crude oil pour more easily. The first hurdle was the electricity utility, which said it would install the necessary supply only if he paid for a new high-tension line for the whole district, at a cost of $20,000. Having found another site with an adequate electricity supply, he discovered he could not import the $100,000-worth of machinery needed because it lacked a Russian certification.

When he had solved that problem, Mr Rumens had to get permission from the local sanitary, ecological and fire authorities in turn. He also had to find a certified contractor to draw up a general plan for the project to take to the Russian standards agency, which would then oversee every detail of the construction work—no doubt finding many more snags along the way. The bribe for avoiding all this would be $50,000. After more than a year, the project—which would generate a dozen jobs, and create a product that Russia could export all over the former Soviet Union—remains stuck.

Corrupt bureaucracy is not a universal blight. There are many examples of clever and determined people dealing with it, at least for a time. Eight million Russians now work in new small businesses, producing—even according to official statistics, which are certain to understate the figure—5% of all industrial goods and 15% of all services in the country. Factories, particularly small ones, are the most vulnerable to officialdom; nimble small firms in the service industry can more easily escape the bureaucrats' clutches.

But the cost of all this obstruction is huge. German Gref, the minister for economic reform, reckons that bad regulations cost the country 167 billion rubles ($5.7 billion) a year. Like all official figures in Russia, this should be taken with a large pinch of salt. But bureaucracy certainly presents the biggest single obstacle to both growth and democracy.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

A reconditioned model

Jul 19th 2001

Russia has changed since Soviet days, but not nearly enough

REFORMING the post-communist system of government is hard. Even the star of the class, Estonia, with all its advantages of history, geography and outside support, is finding it a long slog. For Russia, a country that is almost unmanageably vast and has little experience of the rule of law, private property or public participation, the task is awesome.

Russia's new rulers have made three big changes to the way the country is run. The first has been to recentralise government. The regional outposts of federal agencies such as the tax authorities, the security service, the police and the prosecutor's office are now more or less back under the control of the Kremlin, which helps to counteract over-mighty local barons. Mr Putin has also appointed seven regional governors-general to represent the centre's interests in the provinces. Russia is no longer disintegrating, as it seemed to be during much of the 1990s.

The second big change has been to slap down the tycoon-politicians. Half a dozen big shots from the Yeltsin era have come to grief. They include Boris Berezovsky, a political fixer, and Vladimir Gusinsky, who ran a highly politicised anti-Kremlin media outfit. Both are in exile. Others have remained in Russia, but are licking their wounds. Pavel Borodin, who used to run the Kremlin's property empire and is facing a Swiss bribery investigation, has been shunted downwards to a sinecure overseeing the much-postponed union of Russia and Belarus. Rem Vyakhirev, a former boss of Gazprom, the giant national gas company, has been booted into a non-executive directorship. Yevgeny Adamov, who used to run the atomic power industry as a personal fief, has retired under a cloud, as has his colleague from the fuel and energy ministry, Viktor Kaluzhny. Roman Abramovich, a tycoon and associate of Mr Berezovsky, who seemed to have made a smooth transition to the new era, is now under investigation by the prosecutor's office for fraud and embezzlement.

AP

Berezovsky and Gusinsky: in exile

All this is sending clear signals to other top Russians who operate at the lucrative overlap between state power and private profit. The barons now understand that if they want to keep the assets they gobbled up in the wild years of the 1990s, they have to toe the line. Peremptory cash whip-rounds for Kremlin causes are met promptly and uncomplainingly. Any politicking is low key, usually confined to the regions, and stops at once if it treads on important toes. The rules of the game are broadly the same, but the relative strength of the players has shifted.

If at first you don't agree, try again

The third, and most important, change is often referred to as “consolidation”. The Kremlin is creating a political system that is still recognisable to western eyes, but works from the top down rather than from the bottom up. The media, for example, are much more diverse than in the Soviet era, and there are plenty of lively and intelligent journalists around. With a few exceptions, though, they take the official line on the big issues of the day, and avoid a clutch of taboo topics: the role of the security services, human-rights abuses, especially in Chechnya, corruption in the Kremlin, and any direct criticism of Mr Putin and other bigwigs.

One reason is self-censorship. With so many interesting things to cover, why risk trouble by going for the controversial ones? Journalists who go too far risk beatings or worse. A little of that has a strong deterrent effect on the rest. But there is also direct guidance. Every week, top editors troop into the

Kremlin for a “briefing” that can seem more like an instruction session. Lastly, there is financial and legal pressure: finding or inventing crimes or debts that can be used to squeeze the recalcitrant. The rule of law is so hazy that even a hermit could be jailed or bankrupted.

Consolidation has entered parliament too. Politicians haggle over the details of new laws, but offer little serious resistance. Opposition parties bark a bit, but never bite hard. Only the numerically insignificant liberals of the Yabloko party put forward coherent, consistent criticism. Few Russians get to hear it.

A similar corporatist tune is playing elsewhere. Docile official trade unions are tolerated; independent ones find the climate chilly. Pressure groups and charities are welcome if they complement the state's efforts, but get leant on if they criticise them. Organising, say, a pagan cult can land you in jail. Having finally noticed that non-governmental organisations exist, the Kremlin now wants to corral them into an official “Civil Society Chamber”.

The most unpleasant part of all this is something that looks ominously like state-sponsored xenophobia. For anyone with access to information that might conceivably be considered as sensitive, contact with outsiders is becoming risky. The Academy of Sciences, the most prestigious intellectual body in the country, has instructed its members that all dealings with foreigners must be cleared in advance with security-service officers working in the Academy's administration. Being a foreign businessman, journalist or academic in Russia has become riskier too. An American lecturer in Omsk who asked her students to collect data about local enterprises was denounced by the local goons for endangering the investment climate.

The most unpleasant part of all this is something that looks ominously like state-sponsored xenophobia

As yet, it is hard to nail down what all this amounts to. Civil-rights groups say the country is fast moving back to the Soviet era. Yelena Bonner, the widow of the country's best-known human-rights campaigner, Andrei Sakharov, says Mr Putin is introducing “modernised Stalinism”. That seems prematurely harsh. Except for the ghastly mess in Chechnya, the authorities mostly work by softer methods. They harass people and organisations they dislike, but usually rather ineptly. In June, for example, they prevented a former political prisoner, Sergei Grigoryants, from leaving the country to attend an international human-rights conference in America. Twenty years ago, he would have faced not a day's delay but several years' forced stop-over in a labour camp.

AP

All the news that's fit to print?

There are echoes here of the late Soviet era in East European countries, such as Czechoslovakia, where some nominally independent political parties, organisations, media and other institutions existed, but under the watchful eye of the communist party and the secret police. A real opposition sputtered along, largely underground, sometimes tolerated, but more often harassed or downright repressed.

In Russia, this state of affairs need not be the result of a sinister master plan. Authoritarian habits left over from Soviet and tsarist days are so deeply rooted that they could be sprouting again of their own accord. Some elements, such as the highly restrictive internal registration system, never went away at all. Mr Yeltsin, for all his faults, had a gut commitment to democracy, freedom of the press and friendship with the West, as well as a healthy distrust of the security services. Mr Putin sets a different tone.

The Kremlin and its allies argue that a firmer stance is necessary after the chaotic liberalism of the Yeltsin era. Russia, they say, is too big and too backward to be governed exactly like a western country. Democracy is fine in principle, but it must be managed. To prevent chaos and gradually get people to respect the law, it is necessary first to establish a sense of order and authority, they continue. Only a tightly run state can push through liberal economic reforms, which in turn will create a stronger middle class, which will eventually become the foundation for a solid democracy and the rule of law.

Many, perhaps most, Russians would broadly agree with this, although millions of others (and their friends abroad) who yearn for more democracy and freedom now, not later, find it deeply disappointing. Top Russians like to cite examples such as Chile or Taiwan, which have emerged as prosperous democracies from periods of more or less authoritarian rule. They give less attention to the rather more numerous places (most of Africa, much of Latin America and Asia) where state bossiness has allowed self-interested and incompetent elites to mismanage their country. Russia's own history, its heavy

dependence on easily looted natural resources and the evidence so far all make it seem likely that the country will find itself in the second category, not the first.

Mr Putin's experiment does seem to have made the state a little stronger and quite a lot more stable, but not noticeably more efficient, and certainly no more accountable or transparent. Apart from increasing stability, which is admittedly hugely important, the changes implemented so far have done little to create the conditions for sustainable economic growth. Taking revenge on businessmen and regional leaders who have become too big for their boots creates a superficial impression of decisiveness, but it has severe limitations. First, it does not always work: the Kremlin has come badly unstuck several times when it has stepped into regional elections, only to find itself outmanoeuvred by local power-brokers. At a deeper level, though, the ad-hoc targeting of a few conspicuous culprits makes no noticeable difference to the way the country works.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

States within the state

Jul 19th 2001

Russia's institutions seem designed to ensure that nothing changes

COMPARED with the Soviet era, the Russian state these days is strikingly pluralist. Power is dispersed among the following incumbents:

• **The Kremlin**. The presidential administration remains fearsomely powerful. It is very wealthy, having inherited most of the Communist Party's vast property holdings, including farms, hospitals, aeroplanes, mansions and so forth, which provides it with a big sack of carrots. But the Kremlin lacks real administrative power to make things happen regularly and reliably, especially in the far-flung corners of the bureaucracy.

• **The security services**. The heirs to the KGB have mountains of useful compromising material on everyone, and plenty of lucrative business opportunities, ranging from the outrageously corrupt (smuggling) to the more or less legal (providing security for businesses). Mr Putin has recruited some top people from this source (mostly chums from his own time there), and the services' reach and grip have increased. But their relationship with the Kremlin is uneasy, echoing the edginess between the KGB and the Communist Party in the past.

• **Big business**, chiefly energy and metals. Private property in Russia is not an absolute concept, but depends on the political context. Most owners of former state property got it by underhand means, and could lose it the same way. On a day-to-day level, though, big companies are pretty powerful, with their own security services (usually ex-KGB people) and payrolls studded with ministers, officials and lawmakers.

• **Government ministries**. These are largely autonomous in their everyday decisions, not much good at administration, but adept at extortion; for example, levying bribes from the majority of businesses in Russia that require licences, permits and so forth. The tax and customs services, in particular, stand out for their expertise in this area. Changing anything in the ministries is very difficult. A new minister has little hope of prevailing against the entrenched interests in the lower ranks, and honest and competent replacement bureaucrats are hard to find.

• **Prosecutors**. Hugely influential but heavy-handed, unaccountable and corrupt, they can get almost anyone arrested under Russia's vague and contradictory laws, and usually convicted too. Their powers have remained largely unreformed since Stalin's day.

• **The armed services**. These are much weaker than they used to be, with their morale badly dented by past and present unwon wars in Chechnya. Although there are lots of them (two million plus in uniform), and they have nuclear missiles and other advanced weapons, they are also plagued by accidents, corruption and low morale. The arms industry—heir to the Soviet Union's money-guzzling military-industrial complex—is now showing some signs of revival, thanks to more effective arms sales and renewed subsidies.

• **The Central Bank** is constitutionally independent (a good thing) and therefore lavishly run (not so good), with its own large property empire. It is sniffy about government economic policies on matters close to its heart, such as banking reform, and its views usually prevail.

• **Organised crime**. Less visible these days, gangsters have largely moved into legitimate business and officialdom for a quieter and more dependably lucrative life, but they still have powerful networks of connections.

To make things more complicated still, all the above, far from being monoliths, are ramshackle coalitions of different interests. A similar mix is replicated in each of Russia's 89 regions and republics, where yet another ingredient adds further spice: elected local politicians.

Although every part of this structure is nominally subordinate to the Kremlin in one way or another, in practice the centre's control is limited. Smaller parts of the state apparatus find it hard to assert themselves against some of the big and powerful ones, such as the customs service. Ivangorod's town council, for example, has fought a lengthy battle to clear some Danish sewage-processing equipment donated to it through customs. It has been stuck for months, awaiting payment of an unaffordable fee. Meanwhile the town carries on dumping raw sewage in the river.

Given Russia's new pluralism, it is hard to imagine the Kremlin regaining the iron control it had in the Soviet era, even if it wanted to. But the dispersion of power also means there is now a tendency towards stagnation, because there are huge vested interests against change, even of a moderate and sensible kind.

“The key people are not adequate; it is not organised. We pass the plan and then nothing happens,” complains Igor Lisinenko, a tea tycoon who heads a pro-business grouping in the Duma. Arkady Dvorkovich, an American-educated 29-year-old deputy minister and one of Russia's most impressive reformers, concedes that an efficient state is a must if other changes are to work properly, and that it would have been better to start off with administrative reforms. Unfortunately, he says, this was politically impossible.

So far, the only conspicuously successful change the government has introduced has been a tax-reform package, which on the evidence of the first few months has somewhat raised the tax take, especially from individuals. The reformers have also been able to push through laws on private land ownership, deregulation and other pressing issues. The question is whether these new laws will make much of a difference. Many of the reforms needed in Russia, however essential, are unlikely to have any immediate effect on their own.

Mr Dvorkovich says that by September deregulation should have produced a “noticeably different legal climate” for business. The number of activities subject to licensing will be reduced by 80%. New rules will restrict random visits by inspectors from the despotic health, fire, labour, trade and similar agencies. These are a big source of corruption: some businesses get two or three inspections daily. From next January, registering a new firm should be a question of days, not weeks, with just one point of contact with the bureaucracy, rather than the current parade through dozens of sticky-fingered offices.

How will the bureaucrats react? Senior posts in the world of bribes are so lucrative that they are sold, rather than applied for. This practice goes way beyond the obvious jobs in tax and customs offices. A lowly notary in Moscow, for example, may have to pay $500,000 to open an office which can then be used, extremely profitably, to regularise all manner of shady or even illegal transactions. Top posts in the traffic police are also immensely rewarding. After all, every roadside advertising hoarding and every petrol station depends on hefty regular payments to the local cop or his chief.

In the short term, the chances are that the bureaucrats will simply sidestep the reforms. Clauses allowing added inspections “in exceptional circumstances”, for example, may allow the bribe-hunters to carry on much as usual. The hope, says Mr Dvorkovich, is that once the new laws are in place, Russians themselves will be more prepared to take on corrupt or obstructive bureaucrats. “If people really believe that the state wants to change the situation, then they will not be afraid to report abuses. Now they just pay bribes,” he says.

That slender hope rests principally on reform of the judiciary and court system. Without an independent legal framework that the state itself regards as sacrosanct, why should ordinary Russians take the legal system seriously? The problem is that most judges have spent their careers working, in effect, as junior civil servants in a culture where accusation and guilt amount to almost the same thing. Acquittal rates are well under 1%. All that most courts decide is the length of sentence. Judges are paid less than $200 a month in Moscow and $100 in the provinces; they depend on other civil servants for housing and other perks; and they are very overworked. No wonder that corruption and political meddling are rife. Even the slightly better-functioning parts of the legal system, such as the supreme court, have a very patchy record.

But at least Mr Putin seems to recognise the importance of further legal reform. He has criticised “shadow justice”' and the “privatisation” of the prosecutors' powers. “The country's judicial system is lagging behind real life. Not only for entrepreneurs, but also for many people who are seeking to restore their rights in law, the courts have not been quick, fair and impartial,” he says.

Under the reform drafted by the Kremlin, more judges would be recruited, they would be better paid, and

new rules would be introduced to punish bad ones. Courtroom conditions and back-up would be improved, and the courts, not the prosecutors' office, would be responsible for issuing search and arrest warrants. Jury trials would be extended from the nine regions that currently have them to the whole of Russia.

That will make a welcome change, but it will only scratch the surface of the main problem: the misuse of criminal law at all levels for political or commercial ends. Mr Putin approvingly talks about the "dictatorship of law", a somewhat alarming way of saying that justice should always prevail. Even so, he seems to regard the legal system as part of the government bureaucracy that needs to be made more honest and efficient, rather than something that should be a power in its own right to rival the Kremlin.

Besides, even the modest reforms now being considered may not survive hostile lobbying from the prosecutors, Russia's self-styled champions of legality and state interests. Sabir Kekhlerov, a deputy prosecutor-general, argues openly that Russia is not ready for western standards of justice: "Our people's mentality is different; our perception of justice is different; the respect for the law is not the same," he says.

The evidence suggests, though, that when Russians see a chance of winning justice through the courts, they seize it eagerly. Trade unions, for example, fight thousands of lawsuits against bad employers every year and win a good number of them, especially on appeal. Consumer groups use the law too, and so do businesses fighting unreasonable tax demands. Even in an imperfect system, the nuisance value of a threatened lawsuit is a useful weapon for the weak.

Legal remedies apart, public pressure on officialdom can also produce useful results. The first big practical battle here is over freedom of information. "Without that, nothing works," says Elena Panfilova of the Moscow office of Transparency International, an anti-corruption watchdog. She and others are lobbying for draft legislation on this to go to parliament next year. Once the public sees how its money is being wasted and its rights abused, she argues, it should be easier to exert political pressure on the culprits.

Cleaning up

The second priority is a law on conflict of interest. This goes to the heart of Russia's system of government, in which private and public affairs are intimately entwined. "Corruption in Russia is not a collection of cases of bribery. It is a system of governance," says Ms Panfilova. "It is not business capturing the state: business is the state. They do not need to buy laws. They just get themselves elected and pass the laws they want to have."

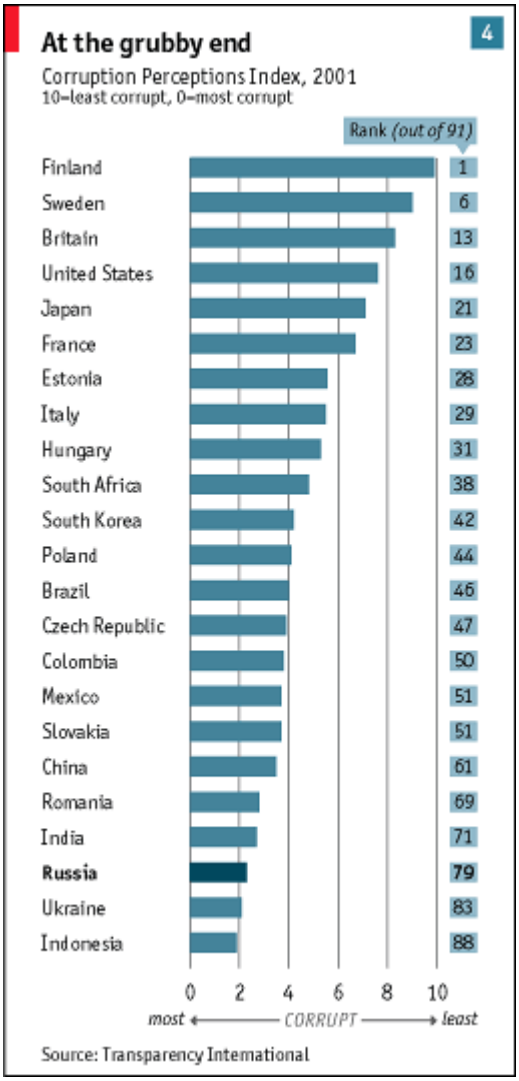
Without a lot of active public support (of which there is little sign so far), the admirable Ms Panfilova and her small but growing network of local allies are unlikely to cause much bother for the most powerful men in Russia. Their best chance of making progress is probably through pilot projects in selected regions. A new administration in Kaliningrad, Russia's westernmost province, has shown interest in a local freedom-of-information law. In St Petersburg, some local building companies have signed an anti-bribery pact.

All these initiatives, state and private, to clean up the mess of Russian state administration may come to something eventually, but not soon. The bureaucracy's huge growth over the past decade continues apace. Most of the people in a position to make changes are those who benefit from things staying pretty much as they are.

Against that depressing background, what chances are there for reforming anything at all in Russia? A slew of other big changes are pencilled in for the coming years. They include the reform of the armed services (bloated and rickety), corporate governance (still piratical), banking (good at money-laundering), and utilities (corrupt and mismanaged). All are vital. None will be accomplished soon. One reason is the sheer complexity of it all.

But a more obvious one is lack of political will. The government has other things on its mind: chiefly, to stay in power.

On the face of it, that seems odd. Mr Putin currently enjoys a 70% approval rating, and the next presidential election is not due until 2004. But the Kremlin is already worried. A law imposing tough new rules on political parties whizzed through the Duma this year. The result will be to make it almost impossible for small, regionally based parties to contest federal elections. The next parliamentary election will probably be brought forward to 2002, a year earlier than planned, to leave a safe gap before the presidential election. The second term, Kremlin people say, will be the time for really tough reforms.



Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Mystery man

Jul 19th 2001

Who exactly is President Putin?

EPA

Wimp, tyrant or moderniser?

THE only man who can get things moving in Russia is Mr Putin himself. But nearly two years after he emerged from the shadows to become prime minister, then president, his motivation and character are still the subject of heated debate.

The thuggish slang, the short temper, the blustering disinformation and the thinly veiled aggression of his early public appearances have given way to crisply delivered speeches about civil society, European integration and the rule of law. In his public utterances, he takes the side of reform, though so far he has delivered more words than action.

Cynics say all this amounts to nothing more than a reshuffle among the corrupt, clannish interests at the heart of power in Russia. Conspiracy theorists think he is the front man for a secret putsch by the security services and others who want to restore Russia's great-power status. The nervous see a nascent personality cult that will ultimately lead to dictatorship.

A more optimistic take on Mr Putin is that he was painfully out of his depth at the beginning, still finds great difficulty in making up his mind, and cleverly keeps out of political fights that would expose his weaknesses. The kindest version is that he is indeed a genuine moderniser, and perhaps even a belated convert to democracy and European values, who is moving very slowly for the simple reason that he cannot go any faster.

None of these theories alone quite fits the facts. If Mr Putin represents a new faction at the heart of power, it is remarkably hard to spot. The security services do have more influence than they used to, but nowhere near enough to make the country a police state. Relations with neighbours, even twitchy ones like the Baltic states, have generally improved since Mr Putin took over. In the provinces, there are isolated examples of a personality cult that has gone way over the top, such as the setting up of shrines in places the president has visited. But the loopiest examples of president-boosting—such as a T-shirted youth movement called “Going Together”—so far seem more ridiculous than sinister.

The more optimistic interpretations do not quite hold water either, especially in Chechnya, where Mr Putin unfortunately shows no shortage of decisiveness—along with ill-disguised contempt for European peacemongers. The strong impression among veteran Putin-watchers is that cosying up to Europe is an affair of the head, not the heart, for the president; quite why, nobody is very sure.

The blistering political jokes now circulating about Mr Putin are mostly of two kinds: those (often recycled from the Brezhnev era) that suggest he is a wimp and a dullard; and those (harking back to Stalin) that portray him as a dictator manqué. The second lot implies that Mr Putin has a hidden agenda that could emerge into the open at any time. On a handful of important occasions, such as a government reshuffle, or the sacking of the head of Gazprom, he has shown he can act with impressive speed. If the current approach of cautious reform does not work, the theory goes, he may well look for a new one. He could yet change gear and speed up reform; or, more worryingly, he could move in a completely different direction, perhaps towards protectionism and renationalisation, or even to a Russian reorientation towards Asian countries such as China and India.

For now, though, the dominant mood in government is steady as she goes. That may look like a low-risk option, but in reality it means Russia just goes on rotting.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Waiting for the crunch

Jul 19th 2001

After decades of neglect, Russia's infrastructure is now in an advanced state of decay

As safe as any Soviet technology

WALKING the brightly lit, well paved, bustling streets of central Moscow, it is easy to think that reform in Russia is now mainly a question of leisurely detail. But take a drive to some miserable town half an hour outside the capital, and the urgent necessity of huge changes stares you in the face. How much longer can Russia's public services, roads, bridges and other bits of public infrastructure survive on their current diet of neglect?

By rights, Russia should have fallen apart already. A large proportion of the buildings and machinery of the Soviet era are hopelessly clapped-out by western standards. By the government's own estimate, 25% of equipment in the public sector is well beyond the end of its design life; according to another official calculation, necessarily vague, 60% of the capital stock is worn out. Investment as a share of national income is still inadequate. Last year at least it grew at a respectable pace, by about 16%, but recently growth has been running at less than half that rate.

The effect of the decline is hard to measure because of two human qualities: ingenuity and endurance. Things that wear out get patched up, again and again. When at last they stop working altogether, people simply put up with it. If they can move somewhere more tolerable, they will; if they cannot, their health will suffer, and they may die early.

The decay in industry is mostly less acute than in public services. For one thing, there is more money about, and there are now clearly defined owners who want to keep their plants running. Services such as telecommunications, petrol stations and flights have improved. Moreover, those Russian businesses that have a chance to compete at all generally need only small investments to open bottlenecks, rather than complete retooling. For the immediate future, Russia's competitive strength, sadly, is making basic products at low cost (for which the existing antiquated machinery is mostly good enough), rather than producing state-of-the-art machine tools, cars or consumer electronics.

Things get more worrying where the surviving Soviet-era technology is highly dangerous: in the nuclear-power industry, for example, or in the military sector. A fairly typical accident was an unexplained series of explosions in June at a rocket base near Moscow, which sent huge plumes of smoke into the air. In May there was a serious fire at an underground bunker that controls Russia's early-warning satellites. Such incidents happen almost every month. The nuclear-power industry is secretive and badly run, but influential and bent on expansion, and has made very little progress on safety since the Chernobyl disaster. But barring another accident, the effect on the public of its dire state is limited. What really bothers people now is the breakdown of public services and utilities.

Take water supplies, for example. In any advanced industrial country piped water is taken for granted. Not in Russia. In many rural areas the system never moved beyond shared standpipes on the street and an earth closet in the garden. But now the combination of a financial squeeze and physical decay is pushing urban life in the same direction.

EPA

Novorossisk should by rights be one of the most prosperous places in the country. Not only does it export a large chunk of Russia's oil, but it is also the terminal for a new pipeline from Kazakhstan. Billions of dollars-worth of the black stuff flow through the port every year. Yet its inhabitants live on the verge of squalor. Piped water runs for just two hours twice a day, when people scurry to fill baths and buckets. There is almost no street lighting, the roads are disgraceful, and the sewage system cannot cope. Life is tiresome, humiliating, smelly, unhygienic.

Similar problems crop up everywhere. Trains run more slowly and get derailed more often; roads are bumpier, power supplies more erratic, roofs leakier, buses and aeroplanes more rickety. Despite it all, life in most of Russia, for now, still seems to muddle along without spectacular disasters, albeit inefficiently and uncomfortably. “Since they cut the electricity off a few years ago, we have been milking the cows by hand,” says a tipsy and exhausted-looking woman in Vasilyevo, a village of a few hundred people in the Pskov region of western Russia.

Home discomforts

Vasilyevo is like thousands of other similar places in Russia: nothing much goes on there, other than subsistence farming in the ruins of the bankrupt collective farm. Has life improved in the past 100 years? Of course, say the locals. It has got worse recently, but most people do have televisions and refrigerators. There is still electricity (for private dwellings), an occasional bus, a just-surviving school, a very basic clinic, a half-derelict “house of culture”. No real reason to complain, then: life is *normalno*—a revealingly ambiguous Russian word that means something between adequate, tolerable and usual, rather than “normal” in the English sense.

Snafu country

On Russia's northern and far eastern fringes, though, life is not even *normalno*. Among people living north of the Arctic Circle, life expectancy is below 50—worse than in many poor African countries. When their heating system broke down last winter, thousands of people in the industrialised, energy-rich and once quite prosperous Primorsky (Maritime) region in far eastern Russia endured weeks of life at –20°C, warmed by nothing more than homemade heaters (such as cooking oil in a tin, with an old rag as a wick). Hospitals filled up with frostbite cases. The federal government flew in pipes and valves for emergency repairs.

Part of the problem is the sheer age of the hardware. The number of serious breakdowns in heating, power and so forth has risen fivefold since the Soviet era. Part is incompetence and corruption. Part is the result of reform so far. Consumers are not willing or able to pay the real cost of their utilities, and energy companies are no longer willing to provide them unpaid.

Last month, for example, the water company in Nakhodka, Russia's main Pacific port, with a population of 180,000, could not find the money to pay Dalenergo, the local power company, which responded by cutting off supplies to the pumping station. The water stopped flowing. After a week, the mayor sent police to reconnect the power.

Russia urgently needs to find a way of bringing more money into public services, both from charges to users and from investors. The government is approaching the problem with an odd mixture of alarmism, complacency and bravery. Officially, it admits to something called the “technogenic problem” that supposedly threatens to shut down many public services and much of heavy industry in 2003. This date seems to have been plucked out of the air to coincide with an inconvenient $18 billion spike in Russia's debt service in that year, with a view to scaring its creditors into rescheduling its loans yet again.

That idea appears to have been quickly dropped again, partly because of western weariness of Russian whingeing, and partly because of the Kremlin's overriding desire to rebuild Russia's financial reputation. But the 2003 problem is also used to attract attention at home. One of Mr Putin's top advisers privately dismisses the idea of a specific problem in 2003 as “nonsense”, but adds approvingly: “This is the first time in the past ten years that people in senior positions have started to think two or three years ahead. The horizon used to be three months at most.”

The government's main practical answer is a planned $20 billion, ten-year reform of communal services, in which subsidies would go direct to poor families, rather than being wastefully paid to the inefficient providers of heat, power and housing. High-income households will supposedly start paying the full costs of such services from next year, low-income ones from 2004. This all sounds very sensible, but the plan, if adopted, is likely to prove politically explosive.

Aman Tuleyev, a paternalist governor from Kemerovo in southern Siberia, was one of many regional leaders horrified by Mr Putin's announcement. He responded:

> Dear Vladimir Vladimirovich, I simply beg you. I beg you on my knees to forbid any games with fire where the population is concerned. We will end up being sorry. There is a simply idiotic psychology whereby if an electric bulb is not lit, then the president is to blame. We need to change that psychology of the population. Everything is piled on the head of the government. Everything is piled on the head of the president.

If it happens, reform of utilities will certainly be the most difficult step Russia has undertaken since the liberalisation of consumer prices in January 1992, which exposed the hyperinflation that was destroying the nation's savings. As with every other reform so far in Russia, it will be the poor who bear the brunt. The harsh new conditions in the labour market hurt the weak most, and so does the deterioration in basic public services.

Communist central planning has left a terrible legacy of whole towns and cities where there is virtually no way to earn a living. These are in inhospitable parts of the country, and used to rely on producing things for which the only buyers were the Soviet war machine or export customers in uncomplaining captive nations. Now those plants are uncompetitive and often derelict. Subsistence farming, which sustains much of the population in southern and western Russia, is difficult or impossible in the harsh northern climate. Inhabitants of these places, along with the one-third of the population elsewhere who live below the poverty line, have two remaining cushions. One is artificially low energy prices: just $12 for 1,000 cubic metres of gas, against a world price of around $132. The other is tiny rents. If those go, destitution beckons.

Given how timid and slow the government has been on implementing reforms, it will be surprising if its shake-up of communal services makes much headway before the next presidential election. More likely, once again nothing much will change, meaning yet more breakdowns and higher costs, and more misery for its people in the long run. No wonder their numbers are dwindling.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Endangered species

Jul 19th 2001

Life for most Russians is bleak, unhealthy and short

EPA

Cut-price oblivion

DEMOGRAPHERS are normally cautious people. When they talk about Russia, though, they start dotting their conversation with words like “catastrophe”. The country's population is increasingly unhealthy, ageing fast and shrinking.

The first problem is that Russians are having fewer babies. Despite a tiny upward blip last year, the number of births per woman is down to 1.17, one of the lowest figures in the world. According to some estimates, it may drop to 1.0, well under half the replacement rate of 2.14. It is easy to see why. For all but the luckiest Russian women, having any children, let alone lots of them, is a passport to poverty and stress. And even those who do want to have families often find that they are not able to. The main means of birth control is still abortion, as it was in the Soviet era. Partly as a result, one-third of women of childbearing age are infertile, according to Murray Feshbach, an American demographer.

Second, Russians die prematurely. Two-thirds of the men smoke, and far too many drink: average consumption per adult is equivalent to 14 litres of pure alcohol a year, more than twice as much as in America. Russians also eat lots of unhealthy food and take insufficient exercise. The result is a high incidence of cancer, accidents, heart disease and other health problems that finish people off early. Russian men on average now live to only 60, compared with 64 in 1991.

The worst is yet to come. The sexual revolution that followed the collapse of communism made Russians' private lives not only more exciting, but also a lot more dangerous. The number of people with syphilis (a good early-warning indicator for AIDS) is shooting up: figures are 100 times higher than the West European average. Mikko Vienonen, an outspoken Finnish doctor who heads the World Health Organisation's office in Moscow, speaks of an impending disaster of African proportions. In a few years' time, he says, there could be 10m Russians with HIV.

Russia's other health problems, which would be worrying enough in other countries, are dwarfed by the havoc wrought by self-destructive lifestyles. Most Russians take their spirits neat. Beer counts as a soft drink. Price is no deterrent: the most expensive ingredient in a Russian Bloody Mary is the tomato juice, and cigarettes cost less than chewing gum. Advertising is ubiquitous, and fatalism rules: condoms are about as popular as seatbelts.

In principle, Russia's public-health catastrophe can be fixed. France and Finland, for example, have managed to tackle alcohol abuse. But the government would have to do all kinds of things it is clearly not good at, such as showing flexibility, imagination and public-spiritedness, pursuing long-term goals, standing up to commercial lobbying and working with charities and pressure groups.

Instead, it has responded with an alarming mixture of complacency and paranoia. The bureaucrats who said that narcotic abuse would never be a problem in Russia now say the same about heterosexual transmission of HIV. Nobody is willing to confront the merchants of death in the alcohol and tobacco lobbies, the prudes and bigots in the Orthodox church, or the stick-in-the-muds and empire-builders in the health-care system.

Russia's tuberculosis epidemic is a prize example. A $100m World Bank loan contingent on the country switching to modern treatment methods, such as carefully monitored drug regimes, remains blocked because the health ministry prefers its traditional methods of isolation in semi-penal sanatoria, followed by surgery. Now the scourge of multi-drug-resistant TB is spreading largely uncontrolled, with horrible consequences for both Russia and its neighbours.

Little grey cells

The third big danger is further deterioration of the education system. It is Russia's still relatively well-educated population, more than anything else, that sustains the belief that this is more than just a large, poor and badly run country.

Young teachers are a rare sight, though the problem is impossible to quantify: the education ministry says it cannot afford to keep statistics on the rise in teachers' average age since 1989. The education that is being provided is still mostly rigid, narrow and old-fashioned, run by entrenched, Soviet-era bureaucrats. Accurate regurgitation is prized over original thought.

The most remarkable thing is that schools still function as well as they do. It is an impressive, even moving, experience to visit decrepit little schools in the provinces where a bunch of dedicated middle-aged women, on tiny salaries and without any modern books or equipment, instil the basics of maths, science and Russian literature into the heads of their pupils. “Schools have been abandoned by the state, but survive because they are part of civil society,” says Artem Yermakov, a thoughtful journalist working on a newspaper for teachers.

In higher education, corrupt methods of gaining entrance and securing better

grades are rife, especially in sought-after subjects such as languages, economics and law. Bright children from poor backgrounds, especially in the provinces—today's young Mikhail Gorbachevs or Vladimir Putins—would now find it very hard indeed to get an education to match their talents.

from poor backgrounds in the provinces would find it very hard to get an education to match their talents

Russian employers confirm that overall standards are falling, especially in technical education. Anatoly Kononov, a young agricultural entrepreneur in Merchanskoye, in the Kuban region of southern Russia, says that newly qualified agronomists are all but useless: “They just go to the institute to say that they have a diploma.” The biggest barrier to growth, he explains, is that even for the equivalent of $300 a month—a huge wage by Russian standards—he cannot find properly trained agricultural experts.

One reason why higher education is nevertheless still holding up fairly well is that Russians have become acutely aware of the value of a good education. Standards are generally still remarkably high, and motivation is higher than it used to be. Information from the Internet partly makes up for geographical isolation and poverty. In a teacher training college in remote Syktyvkar, the unannounced arrival of a British journalist in an English class provokes a lively and well-informed discussion of Rudyard Kipling's novels. Western employers find that the Russian management trainees they recruit are outstanding for their reasoning and analytical abilities, although sometimes their softer skills—such as teamwork and presentation—are less well developed.

Other reasons for the system's survival include the collapse in the birth rate, and the generous staffing levels adopted in Soviet days. Even though many teachers have left the profession, there are still mostly enough to go round.

Nobody knows quite how many ambitious, talented Russians have left for happier shores, but at least a million are reckoned to have gone to Israel, a similar number to Western Europe, mostly Germany, and a slightly smaller contingent to North America. In the 1990s, that exodus was balanced by the 3m or so Russians, usually well-qualified ones, who returned to the motherland from the even worse conditions of the southern parts of the former Soviet Union. Mr Kononov, who emigrated from Kazakhstan to Russia in 1994, made his first fortune in the seamy business of petrol distribution, and is now growing tomatoes and peppers on 2,800 hectares of previously idle land. He speaks lyrically of his adopted region's potential: “It is so much easier here, it is incredible.”

That inward migration has largely halted. Although a trickle of Russians, foreign passports safely in hand, are now returning from the West, overall the brain drain looks set to get worse, not better. And who can blame the émigrés? Other countries, too, have problems such as creaking education systems, ageing populations, ill health, pollution, poverty, bad bureaucrats, regional tensions, uncompetitive heavy industries, cash-hungry public services and terrorism. What is special about Russia is that it has all of them at once.

Barring a radical change at the top, the next few years seem likely to bring a slow but accelerating decline in most of the economy and increasing authoritarianism in politics. In short, Russia will be a weaker country with a rather stronger state. That is making the rest of the world wonder whether it will be nastier too.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

In search of an identity

Jul 19th 2001

Russia is still struggling to come to terms with its new status as an ex-superpower

THERE are three elements in Russia's approach to the outside world. The first is to seek good ties with the West. The Russians have said they are looking for partnership with Western Europe, and for a businesslike relationship with America. To that end, the second element—playing geopolitical games aimed at undermining American world "hegemony"—seems less than helpful. The third is to consolidate Russian influence in the former Soviet empire, especially in the weak, unstable and quarrelsome bits.

The results have been mixed. Trade ties with Europe have become increasingly solid, especially in natural-gas exports. Russia would like to join the World Trade Organisation, which will give the stronger Russian companies a better chance in world markets but let in more competition. On the other hand, inward foreign investment has been disappointing. The total since 1991 amounts to only $22 billion—half the figure for Poland.

AP

Wish we weren't here

The big gap is political. Western attitudes to Russia's behaviour in Chechnya range from concern to horror. The war to restore Russian rule there, prompted by a series of terrorist attacks in August and September 1999, shows no sign of ending. Almost all the top rebel commanders are still at large. Russia's puppet government is on the verge of collapse. The fighting has killed or maimed tens of thousands of civilians; hundreds of thousands have fled their homes. There have been atrocities on both sides, but the balance of blame is overwhelmingly on the much more powerful Russian side. The Kremlin brusquely brushes aside complaints about the many well-documented cases of torture, arbitrary executions, abductions and other outrages that breach numerous international agreements signed by Russia, as well as its own laws and constitution. Critics see Russia's behaviour towards the Chechens as symptomatic of its own decayed and lawless system of government.

As democracy in Russia shrivels, it moves further away from western standards. Despite official insistence that the press is free and human rights are respected, there are legitimate doubts. Some foreigners even question whether Russia should continue to be a member of the G8, alongside the world's seven big advanced democracies.

Fiddle, fumble

The geopolitical games are not particularly successful either. Mr Putin jets around the world to visit former Soviet allies such as Cuba, Libya, Vietnam and North Korea, and cultivates Iran and Iraq. But friendships with poor pariah countries serve little political or economic purpose. Policy towards China and India has been rather more productive. Arms sales are flourishing. Russia has also joined up with five other countries worried by Islamic terrorism (China, Kirgizstan, Kazakhstan, Tajikistan and Uzbekistan) in a security grouping called the "Shanghai six", but to little effect so far.

Russia's patent military weakness (barring possession of unusable weapons of mass destruction, and the ability to sell advanced arms abroad) makes any attempt to flex its withered superpower muscles pointless. Plans announced last year to restore a blue-water navy seem to have been shelved. Russia seems to be giving up its last big overseas naval base, in Vietnam. Attempts to stand up to the West on issues such as Nato enlargement tend to follow a sterile pattern of warnings, tantrums, sulks and grudging acceptance.

The success story, of sorts, is in the inner part of the former Soviet empire, where Russian clout is steadily growing. Fears of Islamic terrorist insurgency have made the countries of Central Asia much more receptive to offers of Russian military help. The other successful policy has been the use of gas debts to gain equity stakes in important industries. Russian influence in Ukraine has risen sharply after a series of political hiccups there in the past year. Viktor Chernomyrdin, the new Russian ambassador to Ukraine (and a former prime minister), is referred to, only half-jokingly, as Mr Putin's viceroy in Kiev.

So where does Russia go from here? The first question is what price Mr Putin is willing to pay to be friends with Europe. Dmitri Trenin, a retired colonel turned pundit, says Russia should accept that its superpower days are over, and try to join countries such as Britain, France and Germany to become another big post-imperial member of the European club. But so far, Mr Putin seems more interested in Europe as a source of modernisation and stability for Russia than as a club with its own demanding rules about democracy and the rule of law.

The second question is about the clash between Russia's economic weakness and its lingering desire to regain great-power status. Russia's western neighbours hope that, when push comes to shove, Mr Putin's craving for respectability will prevent him from doing anything too unpleasant. They do not have much other leverage: thanks to the oil boom, Russia is no longer dependent on foreign loans to stay afloat.

In the short and medium term, the likeliest outcome is that the economy will grow just enough to keep the country from collapsing, postponing any crunch. If so, Russia will stagger on much as it is now: a large, poor, mostly backward place with a maddening habit of wasting its potential. If the decline worsens, though, all the old fears about Russia that haunted the 1990s—disintegration, unrest, loose nukes, disease and pollution—will re-emerge, with even fewer hopes of recovery.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com RESEARCH TOOLS SURVEYS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Sources and acknowledgements

Jul 19th 2001

Good English-language sources include the UNDP, OECD and WHO, as well as the following, which focus more specifically on Russia:

The Jamestown Foundation

Radio Free Europe

The Moscow Times.com

East West Institute

Besides those quoted by name, the author would like to thank the many other people who helped with the preparation of this survey.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Offer to readers

Jul 19th 2001

Reprints

Reprints are available should you wish to order extra copies of the survey. Please send your request to the relevant region:

World-wide (excluding North America):

Rights and Syndication Department
26 Red Lion Square
London
WC1R 4HQ
United Kingdom

Tel: +44 (0)20 7576 8000
Fax: +44 (0)20 7576 8492
E-mail:rights@economist.com

North America:

Rights and Syndication Department
111 West 57th Street
New York
NY 10019
USA

Tel: +1 212 541 0532
Fax: +1 212 641 9808
E-mail:usrights@economist.com

Corporate offers and customised reprints

For corporate reprint orders of 500 or more and customisation options, please contact the Rights and Syndication Department in the relevant region:

World-wide (excluding North America):

Rights and Syndication Department
26 Red Lion Square
London
WC1R 4HQ
United Kingdom

Tel: +44 (0)20 7576 8000
Fax: +44 (0)20 7576 8492
E-mail:rights@economist.com

Future surveys
Countries and regions
Poland October 27th

America November 17th

Business
Mobile Internet October 13th
European business and the euro December 1st

Finance and economics
World economy September 29th

Science, technology and ideas
Illegal drugs July 28th
Peter Drucker on the next society September 15th
Technology in developing countries November 10th
The universe January 19th 2002

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

The technology industry

Big is beautiful again

Jul 19th 2001 | SAN FRANCISCO
From The Economist print edition

Suddenly, scale matters in the high-tech world. This story looks at the new vogue for big firms; another looks at the return of the computer mainframe

Get article background

BOSSES of big high-tech companies have every reason to turn to prayer these days. One after another they are announcing dismal results. On July 17th Intel, a chip giant, said that its sales in the second quarter had fallen by 24% to $6.33 billion. Net profits dropped by a whopping 94% to a meagre $196m, although that drop is somewhat misleading, as the previous year's profits had included a $2.1 billion gain on the sale of investments. The next day EMC, a data-storage giant, revealed that its second-quarter profits were down by 75%. IBM, which released its numbers the same day, did better, but says that the current quarter is tough. And there is more bad news in the pipeline.

It may seem like hell, but perhaps it is only purgatory. In spite of the bad news, big is starting to look beautiful again in the computer industry. Witness SAP, a large German software firm. Only a year ago, it was considered a has-been. Talent and customers fled the company in droves, especially in America. Now the pendulum is swinging back. On July 19th, it announced second-quarter net profits 24% up on the same quarter last year. Former employees, their stock options under water for good, are being lured back by the security of cash salaries. Customers, saturated with reports of dotcom deaths, are turning back to established companies such as SAP, as well as to Oracle and IBM. "I call this 'the return of gravity'," says Hasso Plattner, SAP's chief executive.

Not too long ago, anybody who questioned the religion of the start-up was told they "just didn't get it". Nimble newcomers were supposed to blow incumbents to bits with disruptive technologies. Yet the revolution, it turns out, was less technological than financial. Venture capitalists and the stockmarkets provided start-ups with capital that was essentially free.

Unsurprisingly, talent and media followed the money. But high-tech incumbents and old-economy companies, too, joined the start-up stampede—because they were afraid either of losing their best employees or of simply missing the gravy train. Many firms created a corporate venturing fund, spun off an Internet business or two and bought innovative high-tech gear from newcomers rather than from established suppliers.

The tide turns

In the first quarter of this year, the world changed. America's venture-capital firms invested about $10 billion: 40% less than in the same period a year earlier, a record drop. The market for initial public offerings has snapped shut. Loudcloud, the most recent big Internet-related start-up to launch an IPO, had to reprice its offering twice. It is now trading at around $2, a third of its IPO price. What is more, dotcoms are slowly but surely disappearing from stock indices such as the Russell 2000.

Corporate venturing is also going out of fashion. Almost half the companies that have set up funds in recent years have abandoned the practice, according to a recent survey by Bain & Company, a consultancy—the highest defection rate since the firm began keeping track of executives' favourite management tools. And an increasing number of firms that spun out dotcom subsidiaries are buying them back, including Siebel, a software vendor, and Staples, an office-supplies chain.

Start-ups have accordingly become less attractive places to work. The best indicator may be the behaviour of business-school graduates. Starting a company is no longer what most dream about: instead, they are taking jobs offered by large companies (see article). An entrepreneurship competition at the Haas School of Business at the University of California at Berkeley drew only 65 business plans this year, down from 182 last year.

One after another, top executives who defected from large companies to join start-ups have either returned to the fold or retired. In April, George Shaheen, the former chief executive of Andersen Consulting, now called Accenture, resigned as boss of Webvan, a once admired online grocer, three months before it filed for bankruptcy.

Customers, too, are turning their backs on many start-ups, particularly in enterprise software and related services, fearful of becoming stuck with a product whose vendor has gone belly-up. Analysts even question whether Ariba and Commerce One, two shooting stars in the e-commerce world, can survive as independent companies.

It is not just that buyers want to play safe. Over the past few years, the software and services firms that thrived have been those that innovated, argues Thomas Berquist, a research analyst with Goldman Sachs, an investment bank. As the technology matures, leadership is naturally shifting to the larger companies. "While innovation is still important, experimentation is over," says Mr Berquist.

In telecoms, the flight to size has already claimed several victims. Once-promising new carriers such as NorthPoint, Teligent and Winstar have filed for bankruptcy because they are unable to find buyers or raise new capital. Instead, Wall Street has rediscovered the regional telephone companies, such as SBC or Verizon, only recently derided as telecoms elephants. At Vortex, a leading industry conference in May, the most admired speaker was Joe Nacchio, chief executive of Qwest—for having had the foresight in 1999 to use his new-economy money (overvalued Qwest stock) to buy old-economy assets (US West, the regional carrier with the worst reputation).

In hardware businesses, too, bigger companies are on the offensive. To gain market share, some have started veritable price wars. The most aggressive is Dell, a PC maker, which has pushed for volume at the expense of higher margins—and recently surpassed Compaq to become the world's largest PC maker. Similarly, large telecoms-equipment makers are offering more bargains, making life increasingly difficult for newcomers.

Even on the Internet, small is now vulnerable, as surfers visit fewer websites. In March, users spent 60% of their time online at only 14 sites—compared with 110 during the same month in 1999, according to Jupiter Media Metrix, a research firm. In no other area is the shift more apparent than in online music. EMusic, MP3.com, Myplay and Napster were supposed to put the five big record labels out of business. Instead, one after another, they have been scooped up by incumbents. Vivendi Universal bought EMusic and MP3.com. Bertelsmann saved Napster with a $60m loan, which can be converted into a 58% stake, and recently acquired Myplay as well. The media giants are now poised to control the online distribution of music.

Yet it would be wrong to conclude that technology start-ups are down for good. Most of these developments simply mirror the excesses of recent years. Already, experienced entrepreneurs with good technology are finding it easier to raise finance than it was earlier in the year. And these new start-ups are likely to be much tougher than their predecessors. They will be built to last, rather than merely to be taken public as quickly as possible.

Longer-term trends also suggest that the future still belongs to smaller firms, argues Thomas Malone, professor of information systems at MIT. When gathering information was expensive, he says, it made economic sense for decisions to be made in a few central places. Now, with information technologies driving communication costs ever lower, more and more people can be well enough informed to act independently. And staff tend to be more creative if they are doing their own thing and not following orders.

To be sure, the same information technologies also make it easier to run large companies. And many of the high-tech markets are subject to network effects, meaning that a single firm often tends to win a dominant share. That is why Cisco, Microsoft and eBay have secured more than 80% of the markets for enterprise networking, PC operating systems and online auctions respectively.

In the end, size is not the only issue. In future, the boundaries of a firm could become less important. The more relevant concept may be complex business processes that span many organisations, for example the supply chain of Cisco, an equipment maker that has outsourced most of its manufacturing. At this point, only one thing is sure: the ones that really didn't get it were the new-economy revolutionaries who could only think small.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Computing

Revenge of the dinosaurs

Jul 19th 2001 | SAN FRANCISCO
From The Economist print edition

Are mainframe computers on the way back?

IF THERE is one technology that reflected the spirit of the recent high-tech boom, it was distributed computing. The Internet, the web, the programming language Java, software as a service, peer-to-peer computing—all of it was about spreading processing power across several machines, often in different locations. This new computing model was said to be cheaper and more flexible than the old approach of central processing by mainframes.

But with the economic downturn, things may be swinging the other way. A number of technology analysts, such as Gretchen Teagarden of Salomon Smith Barney, an investment bank, have detected a "renewed interest in centralised computing". In short, mainframe computers may be making a comeback.

There are good reasons for thinking that the shift might happen. One driver is cheaper communications costs, mainly because of the current—and probably lasting—bandwidth glut, which removes one incentive to put computing power close to the user. More importantly, companies need to cut information-technology costs. One way is to scrap their huge banks of server computers, many of them underutilised, and to run their applications more efficiently on mainframes instead.

Ironically, this is made possible in large part by a program that would have never seen the light of day without the Internet: Linux, the free operating system written by volunteer programmers across the globe, who communicate mainly by e-mail. IBM has adapted the software to run on its mainframes—not just a single copy at a time, but tens of thousands of copies simultaneously, if need be. These huge computers can replace entire server farms—becoming, in effect, ready-made data centres.

This is an attractive proposition, particularly for firms that have some spare capacity on their mainframes. They could use it to run virtual Linux servers. That brings two kinds of benefits. They save energy, floor space and staff—and they benefit from the reliability of mainframes.

This is what an increasing number of firms are doing, according to IBM. It is also one reason why the company's quarterly results, released on July 18th, were better than those of most of its competitors.

Even if one discounts this explanation as somewhat self-serving, there is no doubt that many companies are experimenting with Linux-on-mainframe. Most of them have moved simple applications such as web or e-mail servers to their mainframes. For instance, Winnebago Industries, a large maker of motor-homes, recently threw out its distributed e-mail system and replaced it with a Linux version. But some are going further. Korean Air has just finished implementing a program that keeps track of flight schedules and does revenue accounting.

So is Big Iron, as mainframes are known in IT-speak, poised to reclaim the place at the centre of the computer industry that it lost in the 1980s? Probably not. Many applications are better suited for a distributed computing model; or they do not run on Linux. And the high-end, mainframe-like machines sold by Hewlett-Packard and Sun Microsystems also allow firms to consolidate servers. But the mainframe-Linux combination certainly suggests that computing is not inevitably heading towards an increasingly decentralised model, as so many enthusiasts once used to claim.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Swissair

A scary Swiss meltdown

Jul 19th 2001
From The Economist print edition

How a dud strategy brought a solid company to the brink of bankruptcy

IT WAS a narrow squeak. On July 17th Swissair and the Belgian government, which between them own Sabena, Belgium's national flag-carrier, reached agreement on injecting another *euro*430m ($366m) into the troubled airline. The deal puts a cap on Swissair's liability and closes a dark chapter in its recent history. But the airline remains in dire straits. On July 18th, Swissair's share price bounced up 17% off the bottom of the deep gully into which it has fallen from its alpine peak in 1998.

Under the terms of this week's deal, Swissair will retain its 49.5% holding in Sabena. But the reward for putting up 60% of the extra finance is that it is released from an obligation to pour money in to take its stake up to 85%. The Swiss carrier is also taking nine surplus Airbus aircraft off Sabena's hands, in another cash boost for the loss-making Belgian airline. Athough the European Commission may seek to stop the extra state aid that Sabena is getting, the deal averts the threat to Swissair of a lengthy legal battle with the Belgians.

The Sabena investment was the worst of a series of blunders that had threatened to drag down a once proud airline. Until the late 1990s Swissair was one of the most admired airlines in the world, famous for punctuality and superior in-flight service. It was financially stable. In many ways it was a microcosm of the country whose flag flies on its airliners' tails—solid, reliable, orderly and successful. Like the Swiss army knife, it was an emblem of rugged dependability. Today it is struggling to avoid going bust, with losses last year of SFr2.9 billion ($1.7 billion) and debts of SFr7.8 billion, more than six times the value of its equity.

After the discredited old management team had left in a hurry in April, Mario Corti, the respected finance boss of another Swiss icon, the Nestlé food group, was brought in to rescue the airline. Last week he signalled the sale of more assets in an effort to lop at least SFr3 billion off the company's debts. Instead of a sprawling aviation conglomerate, Swissair (it has gone back to its sensible original name after calling itself SAir for a decade) will consist of the airline and its regional offshoot Crossair, plus Gate Gourmet, its catering subsidiary, and Nuance, its retail arm. Its hotel business has been sold, its information-technology activity is being folded into that of Lufthansa, Germany's flag-carrier, and its rail-catering business will go to Britain's Compass group in exchange for its airline-catering assets. Some belt-tightening and job cuts aim to save SFr250m in annual operating costs. If it fails, the group may have to sell part or all of its profitable catering and retailing companies, the only parts that are doing well.

The culprit in this tale of doom was a disastrous expansion programme, especially a decision to buy stakes in a string of other European airlines. Life was always going to be hard for Swissair as aviation became more competitive with European liberalisation. Europe has 28 scheduled airlines, excluding small regional ones: a ludicrous number. America, a bigger air-travel market, has seven big ones. Mid-sized carriers such as Swissair or Sabena have a problem: they are neither big enough to be market leaders, nor small enough to fit into a niche.

Swissair's other problem is that it is based in a high-cost country and, because Switzerland is not a member of the EU, the company does not have the freedom to expand alone in Europe. It experimented with global alliances, only to see them collapse: Austrian Airlines and Singapore Airlines deserted its Global Excellence alliance, and Delta Air Lines abandoned the subsequent Atlantic Excellence.

Advised by its long-term consultants, McKinsey, Swissair thought it had another strategy. Under the banner of the "Qualiflyer" group, it sought links with other small European airlines: Sabena in Belgium; three small French carriers, Air Littoral, AOM and Air Liberté; LOT Polish Airlines; LTU in Germany; and TAP, Portugal's flag carrier. It also hooked up with South African Airways. These partners would become

customers for Swissair's catering and other aviation-service subsidiaries.

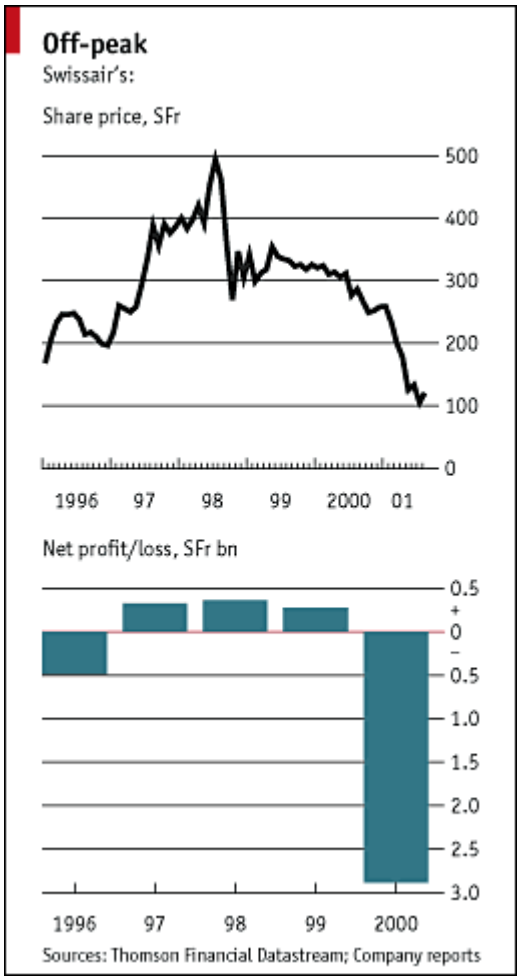
There were a couple of problems with all this. Because Swissair is not in the same league as Lufthansa, Air France, British Airways or KLM, it had to woo other airlines to join its club. It did this by buying stakes in them. Altogether Swissair spent more than $1 billion on such stakes, on top of a similar amount building up its catering operation to make it second only to Lufthansa's. One condition of each deal was that partners switched to Swissair companies for all services. In effect, Swissair was buying customers for the aviation-service businesses it was also acquiring.

But the real clincher was that nearly all the airlines it was buying into were in deep difficulties. The French ones could not compete with Air France or with France's high-speed trains, and they had grumpy unions. So they had hopelessly big losses and little freedom to cut costs to eliminate them. Sabena was heading down even as Swissair bought into it. Swissair's plan to build up Brussels as a regional hub for European traffic did not work, as passengers within Europe stuck to their preference for direct flights. Add to that failure Sabena's overmanning and difficult staff unions—and the chances of Swissair ever turning it round always looked slim.

The problems at Sabena and the French trio damaged Swissair just as its own airline went into loss, because it could not cut costs fast enough to keep pace with falling profits per passenger, brought about by more competition. Even the regional airline, Crossair, which has a good route network, is losing money. Most of last year's SFr2.9 billion loss was caused by provisions against its investments in Sabena and the others.

Mr Corti has thrown this disastrous strategy into reverse, extricating Swissair from France, and thus putting an end to the annual outflow of nearly SFr1 billion to prop up the ailing French trio. Likewise, this week's deal means that Swissair will have no further financial commitments to Sabena.

However, Mr Corti admits that he is still walking a financial tightrope. Since the beginning of the year, Swissair's shares have fallen by some 54%, to give it a market valuation of barely $800m (see chart). Yet the group has spent nearly $2 billion buying airline stakes and service companies. At least this week's Belgian deal draws a line under this disaster and offers Mr Corti some hope of pulling Swissair out of its nosedive. And McKinsey no longer works for the company.



Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Black empowerment

Skin deep

Jul 19th 2001 | JOHANNESBURG
From The Economist print edition

Admirable in theory, but difficult to put into practice

SEVEN years after winning political power, most black South Africans still lack the economic variety. That was the conclusion of a recent commission of inquiry into black empowerment. Reforms, it declared bleakly, have had “almost no impact on the lives of the majority of black people”. So has the experiment failed?

On the face of it, no. Look, for example, at the man in charge of the commission, Cyril Ramaphosa. He turned down a place in government and is now the country’s richest black tycoon and boss of a listed company, Johnnic Holdings, with thriving media interests. He is on the top of the pile, but there are others. A new mixed elite is replacing the whitewash of a decade ago.

The likes of Mr Ramaphosa made their pile in the first phase of empowerment, when big white-owned conglomerates, such as Anglo-American, a mining company now listed in London, unbundled parts of their business to black investors who had borrowed money to buy shares. But that phase is over. Many of the new black rich suffered when their firms’ share prices tumbled on the Johannesburg Stock Exchange (JSE). In 1999, “black-chip” firms accounted for a surprisingly high 6% of the value of the exchange, but by February of this year (the most recent month for which reliable figures exist), they had slumped to below 2%.

Mr Ramaphosa’s Johnnic accounts for most of that, says BusinessMap, a Johannesburg consultancy. Worse, some companies, such as New Africa Investments Ltd (NAIL), a media and financial conglomerate, are in trouble. Once seen as the great black hope, NAIL lost its chief executive, Dikgang Moseneke, in June, and is now struggling to split into separate, more manageable, companies. With such turmoil around, investors are unlikely to finance another black-power spending spree.

One rare bright spot for black empowerment is the petrol industry. Within a decade, the government wants a quarter of it to be black-owned. On July 4th Shell South Africa said it had sold 25% of its oil retail and marketing business to Thebe Investment corporation, the country’s first black-run oil firm. This followed a deal by Engen Petroleum, one of the largest oil-marketing companies in the country and a subsidiary of a Malaysian company, Petronas, to sell 20% of its shares to a black-empowerment company, Worldwide African Investment Holdings.

Yet share deals, whether failed or successful, do little for the mass of poor South Africans. A few chocolate sprinkles on a cappuccino do not hide that it is white froth floating on the top. So the focus of a second empowerment effort has been to get more black people into jobs, especially senior ones.

Where government calls the shots, for instance in state-owned utilities, the proportion of black workers has grown. The share of non-white workers at Telkom, the national telecoms company, has risen from 46% in 1994 to 56% now. If the government manages its long-promised sale of the utilities—Telkom’s privatisation is due within a year—that could bolster black presence in the private sector too.

The government is also using the law. Two acts of parliament, in 1998 and last year, told firms that employed more than 50 people to hire more women, blacks and disabled. State spending, worth 100 billion rand ($12.5 billion) a year, also boosts black businesses. A Preferential Procurement Framework Act passed last year lets government favour black bids for tenders. This has only been partly successful: wily white-owned companies have simply teamed up with black partners to win contracts. Mannie Hirsch, a consultant for empowerment deals, estimates that the practice, known as “fronting”, accounts for 40% of all government tenders.

Neither laws nor procurement rules have yet led the private sector to create enough jobs to mop up black unemployment: around 44% of blacks, but only 7.5% of white, are out of work. Worse, these disproportionate unemployment rates have hardly budged for the past five years.

A third way

Now a third kind of empowerment is becoming popular: encouraging black-owned small businesses. It is far harder to measure progress among unlisted companies, but some anecdotal evidence suggests that black retailers, car-traders and farmers may be doing well. In the conservative wine industry, the first vintage from the first black-owned vineyard, a wine called New Beginnings**,** is due this year. In June, mining companies struck a deal with the government to encourage more small-scale, black-owned mines with a $100m fund.

However, the government's efforts may have done more to boost white small businesses than black ones. Whites blocked from jobs by affirmative-action rules have set up their own enterprises, employing fewer than 50 people to avoid the strictures of the new labour laws. With more education, savings and support from banks than their black counterparts enjoy, they are creating technology, retail and tourism companies, says Kevin Wakefield, head of South Africa's chamber of business. "We have 40,000 small companies, with an average of 30 employees. There has been a huge growth in small white businesses since 1994." Astonishingly, Mr Wakefield says that "significantly less" than 5% of his members are black, although the chamber is planning to merge with a black chamber soon.

Such efforts to nurture activity from the grassroots up will probably bring more substantial change than a few high-profile deals. So the government is likely to be selective when considering the commission's proposals for the next decade. One of these is to set targets. By the end of the decade, the commission suggests, 30% of productive land should be in black hands; 25% of the JSE's shares black-owned; and at least half of government tenders should go to genuine black companies. These goals will be difficult to meet. "The risk is that we get legislative quotas," says Reg Rumney of BusinessMap. "Companies really want to avoid this."

The commission also wants government and business to do more to improve the quality of education and training for black workers; to encourage black involvement when state companies are sold off; and to measure the growth of black economic power in companies not listed on the JSE. "It will take another 30 years to turn things around, and there is no masterplan," says Mr Rumney. The experiment's final results will be a long time coming.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Iranian privatisation

A mess

Jul 19th 2001 | TEHRAN
From The Economist print edition

How not to build a private sector

UNTIL four years ago, it would have been unthinkable for the shoemakers of Shadanpur and the textile workers of Jamco to go out of their way to embarrass Iran's parliamentarians. Those were the days when both factories were owned by a secretive and autonomous state conglomerate called the Bonyad (or foundation). Now, however, Shadanpur and Jamco have been privatised, and their new owners have stopped disbursing salaries.

Staff at Jamco have not been paid for 11 months. On July 15th workers from both factories demanded to be reabsorbed by the Bonyad—though they came off worse in a ruckus with riot police at the parliament's gates. This is not what the bureaucrats trying to pep up Iran's sluggish privatisation drive wanted to hear.

The Bonyad built an empire out of companies and properties confiscated after the 1979 Islamic revolution. At its peak, it employed some 70,000 people in businesses doing everything from running an airline to making tomato ketchup. It reportedly accounted for as much as half of Iran's non-oil economy.

As its full name—the Foundation for the Dispossessed and War Disabled—suggests, the Bonyad was born with a big heart. Its companies were deliberately overstaffed, and capital investment took second place to providing employment, health care and housing for crippled ex-soldiers. In return, the Bonyad was allowed more privileges than the rest of the public sector. It was placed under the direct control of Iran's unelected supreme leader, and it was exempted from tax.

When Mohammad Forouzandeh, a former defence minister, took charge of the Bonyad in 1999, he announced that 80% of its 350-odd companies were losing money. He promised to privatise 250 companies, and to remove the whiff of corruption and inefficiency that pervaded several of them. In fact, the privatisation drive has offloaded only 37 companies, including those sold by Mr Forouzandeh's predecessor. Now, it is said, auditors are poring over the Bonyad's accounts, and some 30-40 senior managers have been sacked. But nobody expects any findings to be made public.

The Bonyad's privatisation drive illustrates all the difficulties that face Iran's hesitantly modernising economy. There has been the odd bright spot: for instance, France's Castel bought Damavand, Iran's biggest mineral-water producer, from the Bonyad. More typical, however, was last year's privatisation of the Rey textile factory, in south Tehran. Workers there say the factory was sold for $2,500; in exchange, the new owners agreed to take on $10m worth of debts. Four months later, money for wages and raw materials dried up. In May, when one of the new owners paid a visit, the workers roughed him up.

Buying a Bonyad company generally means taking on a business suffering from ancient machinery, far too many staff and years of mismanagement. No wonder some privatisations have aroused suspicion. According to Iraj Nadimi, chairman of parliament's economy committee, some new owners are interested less in running factories than in selling machinery and land to make a fat profit.

He may have in mind Gholam-Reza Rasekh, Shadanpur's present owner. For some time after he stopped paying his workers' wages eight months ago, Mr Rasekh denied accusations that he intended to bankrupt the company, and then sell the land on which it sits. He demanded that 220 workers take voluntary redundancy. They refused, and on July 11th he duly declared that he was dissolving the company.

It is not only workers in plants that previously belonged to the Bonyad who are suffering. According to Ali-Reza Mahjoub, a parliamentary deputy and trade-union official, some 80,000 workers in privatised companies are not being paid regularly. But the government has only itself to blame. The high rate of unemployment—well over 20%, according to independent economists—has made it reluctant to repeal punitive labour laws that discourage genuine entrepreneurs. Instead, the government has ended up throwing money at the privatised hulks. In May, the cabinet approved a rescue for private textile factories. Shadanpur's workers have survived on hand-outs from a state-funded trade union. Even Mr Rasekh received a government loan. Those renationalisation calls may not be so unrealistic after all.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Management consultants

Winners' curse

Jul 19th 2001
From The Economist print edition

Consulting firms are suffering from an overdose of talent

FOR years, McKinsey has been warning its clients about the intensifying war for talent. Skilled people are rare, the consultants have argued, and you have to work hard to get them and to keep them. Now it seems to have heeded its own advice so well that it has a surfeit of talent. It has stopped recruiting graduates in Britain and North America. The war has been won—but how to win the peace?

McKinsey is not alone in its *embarras de richesses*. Two other firms, A.T. Kearney and Booz-Allen & Hamilton, have also stopped hiring, while Accenture (formerly Andersen Consulting) is trying to persuade its staff to take sabbaticals. Most firms are increasing their amount of *pro bono* work.

The problem has two main causes. First, consultants are finding that their rate of attrition—the rate at which people leave voluntarily—has shrunk dramatically as rival jobs (such as joining an Internet start-up or a venture-capital operation) have become less attractive. Accenture's rate of attrition is now about 12%; last year it was over 20%. McKinsey's has likewise fallen from around 20% to less than 12%. As a result, the firms misjudged how many people they would need to replace.

Secondly, consultants have become almost too attractive for their own good. After the dotcom meltdown, students are looking for the sort of safety that they provide, says Universum, a Swedish research firm which tracks the career preferences of graduates worldwide. According to its latest survey of American MBA students, five out of their top ten "ideal employers" are management consultancies (see table). Most of the top consulting firms have moved up the Universum table this year. McKinsey, which has been in pole position since 1997, can climb no higher.

This surge in popularity has come at an awkward time for many firms. Although their business is supposed to be acyclical—in demand in both good times and bad—they are finding that the current global economic slowdown is affecting them more than they had expected. Accenture, for example, which went public in New York this week, reported a 32% fall in its partnership income for its latest quarter, even after excluding one-off charges for its rebranding. Both Accenture and KPMG Consulting, which went public in February, have reduced their revenue growth forecasts sharply. Jim Copeland, boss of Deloitte & Touche, says his firm expects a 12% growth in consulting revenues this year, sharply down on last year's rate.

Ideal employers
Companies American MBA graduates would most like to work for

	Rank 2001	Rank 2000
McKinsey & Company	1	1
Boston Consulting Group	2	4
Cisco Systems	3	7
Goldman Sachs	4	3
Bain & Company	5	5
Accenture	6	13
Booz Allen & Hamilton	7	8
Intel	8	12
Hewlett-Packard	9	22
Morgan Stanley Dean Witter	10	9

Source: Universum

Some blame the climate of uncertainty for the slowdown. When businesses at last realise that things are going badly, they will "call in the consultants to get them out of the mess," says one optimist. "But we haven't reached that stage yet," he adds. "Right now, everything is on hold."

The slowdown has been milder in continental Europe than in Britain and America. Firms such as BCG and Roland Berger are still recruiting in Germany. The late arrival of the Internet, and the deregulation of such industries as electricity and gas, continue to stimulate European demand for consultants. But even on the continent times are getting leaner. For example, A.T. Kearney invited its potential German recruits to a luxury resort in Majorca last year. This year, the venue was a frugal hut in the Austrian mountains.

In America, margins are also coming under pressure. "Today, you can hire McKinsey for what it would

have cost you to hire A.T. Kearney a year ago," says Alden Cushman from Kennedy Information, a researcher on the industry. Some firms are showing the pain. Arthur D. Little, one of the oldest, reported "material cash difficulties" earlier this year, after it had to cancel the initial public offering of C-quential, its media and technology subsidiary. It is now being sued by PA Consulting, the largest British management consultancy, over the firms' failed merger negotiations.

Consultants have traditionally been reluctant to lay off staff, and that has been a key part of their strategy in winning the war for talent. But if the slowdown in their business continues, it will take deep pockets to hold on to their gains. Kennedy Information expects worldwide revenue growth to slow to 7-10% this year, but to average 12 % a year over the next five years. Given that it takes several years to train a consultant, firms have a big incentive to hold on to their talent until the next upturn. Last month's call by McKinsey for more capital from its partners should help it, for one, to take the longer-term view.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economist.com BUSINESS
PRINTABLE PAGE VIEW SPONSORED BY
About sponsorship

Drugs

Marketing madness

Jul 19th 2001 | NEW YORK
From The Economist print edition

Prozac by any other name

IRRITABILITY, sudden mood changes, bloating? Ladies, if you suffer from these nasty symptoms just before your monthly period, you could have Premenstrual Dysphoric Disorder. Sounds serious? Eli Lilly certainly hopes you think so. You may never have heard of PMDD, but the American drug company wants you to take a pill for it. Prettily clad in a feminine pink and lavender capsule, the new drug is called Sarafem.

Lilly says that 3-5% of women of child-bearing age—3m in America alone—have premenstrual symptoms so severe that they interfere with daily life. Now Lilly's website boasts that Sarafem "is the first and only approved prescription treatment for both the mood and physical symptoms of PMDD".

But if PMDD is so serious, why hasn't some clever scientist developed a pill for it before? Surely the men in white coats would have been keen to find something to soothe irritable women? The truth is that Sarafem was not invented to cure a hidden problem—an article last month in *Harvard Mental Health Letter*, a health newsletter, points out that PMDD has not even been accepted as a psychiatric disorder. In fact, Sarafem is not new at all. It is Prozac, Lilly's blockbuster antidepressant drug, masquerading under a different name.

Lilly's patent on Prozac—one of the most profitable and heavily marketed drugs ever—is due to expire in August. Though Lilly insists that the timing of the launch of Sarafem is coincidental, its patent, which runs until 2007, will help Lilly offset the loss of high-margin branded Prozac sales to rivals selling cheaper generic versions. This is because the patent does not let doctors substitute generic prozac for Sarafem for patients diagnosed with PMDD.

The reason for the name change is that women who do not consider themselves depressed or mentally ill are reluctant to take Prozac. Fair enough. After all, women who suffer from premenstrual mood changes and physical pains may be helped if they try Sarafem. However, many regard Sarafem's launch more cynically. Some folk complain that the TV ad for Sarafem, showing a woman snapping at her husband, is patronising.

Doctors also worry about the risk of overdosing, because only the small print tells women that Sarafem and Prozac are the same drug. Others are concerned about the trend for people to pop pills for problems that would otherwise not have been thought serious enough for medication. For its part, Eli Lilly seems to be trying to engineer a smart marketing coup. Whether PMDD is real or not, women beware. Those men in white coats really are after you.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Face value

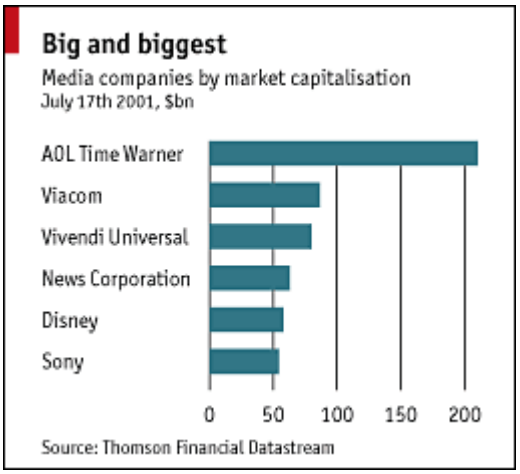
The unknown media mogul

Jul 19th 2001
From The Economist print edition

Can Bob Pittman demonstrate what the world's biggest media company is for?

WHEN AOL and Time Warner grabbed the headlines with their mega-merger 18 months ago, he sat on the podium. But his was the face that did not grace the morning papers, the name that nobody could quite recall. Yet Bob Pittman, co-chief operating officer, is now beginning to emerge from the shadow of his bosses, Steve Case, chairman, and Gerald Levin, chief executive. The scale of the task facing him, as the man whose daily job is to bash the two parts of the media giant together, and so justify to sceptics the group's very existence, was neatly illustrated by the markets' response to the group's second-quarter results, unveiled on July 18th. The shares dived by 9%, even though earnings before interest, tax, depreciation and amortisation had jumped by 20% over the previous year, to $2.5 billion, and the group's pre-tax loss had fallen by nearly half, to $385m.

In sheer operational terms, merging AOL and Time Warner has been hard enough. With a market capitalisation of $210 billion, AOL Time Warner is more than twice as big as its nearest rival (see chart). More than 200 miles (320 kilometres) separates its two head offices: AOL's in northern Virginia, where Mr Case is based, and Time Warner's in Manhattan, the home of Mr Levin. The group employs 90,000 people. One of Mr Pittman's first tasks was to trim the payroll, which he did unapologetically, by 2,400.



What complicates Mr Pittman's job is that, in the past, Time Warner was run as a collection of independent fiefs. Managers were used to getting on with their own thing, meeting together only every other month or so. Mr Pittman, who has moved from Virginia to the merged group's headquarters in New York, summons all unit heads every two weeks. They are lectured not only about hitting their own revenue-growth targets, which are aggressive, but about how they must integrate their businesses with AOL.

Unsurprisingly, not everybody on the creative side appreciates being bossed about by upstart Internet geeks from Virginia. There is a wide cultural gap between the restless 20-somethings from AOL, and New York institutions such as the 78-year-old Time Inc, which owns titles from *Fortune* to *Sports Illustrated*. There is much grumbling among journalists, whether at *Time* or at CNN, about a new tightness with money, and the fears this has prompted for editorial quality. "I never ran the company by numbers," snapped Ted Turner, CNN's founder and patriarch, to the *New Yorker* recently.

To his advantage, the 47-year-old Mr Pittman, son of a Mississippi preacher, does not quite fit the caricature of the techno-nerd dispatched from AOL to sort out the creative types. He was raised in the Time Warner culture, where he worked in the 1980s and again in the early 1990s, when he ran its amusement parks, before moving to AOL via a stint in property. Mr Pittman not only has a reputation as a shrewd, hard-nosed operator; he also has creative credentials. As a long-haired, bearded teenager, he skipped college to become a disc-jockey. In 1981, as a more conventional suit, he dreamed up and launched MTV, now part of Viacom.

Synergistic girl

Perhaps Mr Pittman's biggest challenge is to show what exactly the AOL Time Warner merger is all about. His initial answer is well-rehearsed: "synergies". Take Madonna's current world tour, the first in eight years by the pop star, who is signed up to the group's Warner Brothers Records. First, AOL lured new subscribers by giving them the chance to buy advance tickets. Now, AOL is selling subscribers a Madonna "pass", which lets them see unreleased photos and videos. In August, HBO, the group's pay-television channel, will broadcast her Detroit concert live.

The underlying business model is not simply to wring more money from any one brand. It is to create a "community" of subscribers, of whom the group now boasts a massive 135m; AOL alone added 1.3m of them in the second quarter. Each subscriber is then tempted to buy extra stuff. So AOL will market to its "members" AOL Music, once this is launched as a subscription service for downloading music later this year. All the while, cross promotion drives down the cost of acquiring new subscribers. AOL already sells 100,000 subscriptions to *Time* magazine each month.

No sooner has Mr Pittman enthused about this idea, however, than he insists that the company is not about to hog its content, or its distribution pipes, all to itself. "We firmly believe in non-exclusivity," he declares. Part of this is a ritual appeal to the regulators, who will firmly resist any effort to block access. But it also makes commercial sense: a subscriber to AOL Music, for instance, will want to be able to buy tracks from all artists, not just those signed up to Warner Music labels.

But, if the model is non-exclusivity, then why does AOL need actually to own the music, or the film studio? Why not sign a series of deals with independent content providers? The smooth-talking Mr Pittman does not miss a beat: "because combining the assets in one place gives you the critical mass that allows you to take risks." It also, he adds, "increases your pace of innovation, because companies within the group share their knowledge freely." In other words, had AOL not got its hands on a music division, it might not have thought of setting up a music-subscription service. "Back at Time Warner," argues Mr Pittman, by way of comparison, "we'd never have started MTV without Warner Music."

Perhaps. For now, the case is unproven. The single-minded Mr Pittman may be unusually determined to make it work. He drives his wife crazy by waking in the night to jot down ideas on a bedside notepad. "I sweat bullets," he declares: "I've never taken more than two weeks' vacation a year since I was 15 years old." Hard work, however, may not be enough to change deeply held attitudes. As a boy from Mississippi, that is something Mr Pittman should know.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Mortgage-lending agencies in America

Big scary monsters

Jul 19th 2001 | NEW YORK
From The Economist print edition

Fannie Mae and Freddie Mac are a huge presence in the financial system. Not before time, efforts are being made to rein them in

THE driving force behind what little economic growth is now taking place in the world is, you might argue, America's housing market. The main impact of the Federal Reserve's six interest-rate cuts so far this year has been to trigger a slew of mortgage refinancings and other borrowing against the value of homes. This, in turn, has put extra cash in the hands of consumers, enabling them to spend more than might otherwise have been expected in the face of a sharp economic slowdown. It has also kept house prices strong—outside San Francisco and New York, two cities that are peculiarly sensitive to the stockmarket's fortunes—creating a benign "wealth effect" on consumer spending. That has taken much of the sting out of the malign effect of falling share prices.

The main transmission mechanism between Fed rate cuts and the home owner are some mortgage-lending agencies with significant, though opaque, government backing: Fannie Mae (the Federal National Mortgage Association) and Freddie Mac (the Federal Home Loan Mortgage Corporation). These buy and issue mortgages, which they then securitise by bundling together by the thousand and selling in the debt markets. Between them, Fannie Mae and Freddie Mac either own, or insure the risk on, 40-45% of America's residential mortgages. Combined, their mortgage assets are now two-thirds as big as America's publicly traded government debt. Some analysts think they are on course to exceed public borrowing by the government by 2005. Indeed, given the strong and growing investor belief that the government will never allow Freddie or Fannie to fail, there is a case for viewing their borrowings as de facto government debt.

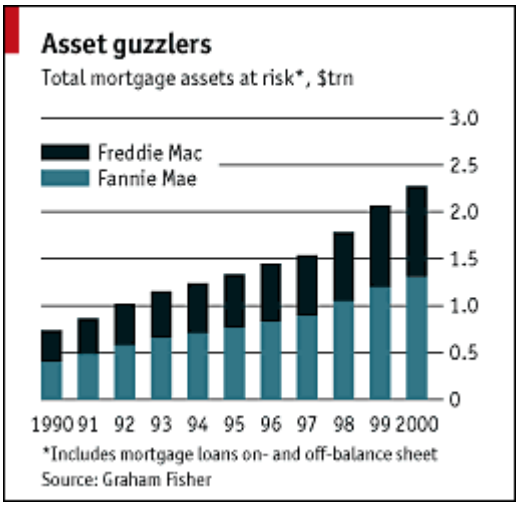
The agencies run a formidable lobbying operation in Washington, yet their financial clout is coming under political scrutiny. In the past few weeks, George Bush's administration has taken a tougher stance towards them, albeit one whose effects will not be felt so swiftly that America's economic problems are made worse. On July 17th the administration backed new, more prudent rules for risk-based capital adequacy, due to bite in a year. It also talks privately about measures to put competitive pressure on Fannie Mae and Freddie Mac, by licensing new rivals.

The spectacular growth of Fannie and Freddie is troubling in several ways, both practical and theoretical. Their activities certainly help to keep the economy above water. Yet, says John Lonski, an economist at Moody's, a credit-rating agency, the economy relies too much on a single sector, housing, to avoid recession.

Much of the increase in housing debt has happened because people have borrowed against the equity in

their homes, ie, against the value of the properties minus existing mortgages. This way, owners are more exposed to a fall in house prices. And house prices might well fall, should the economy move decisively into recession, which is still a risk (see article). Mortgage debt in America is now $5.1 trillion, up from $3.4 trillion in 1995.

Giant mortgage lenders, in effect guaranteed by government, distort the economy's allocation of capital, argues Bert Ely, a Washington-based economist. Indeed, there may right now be the makings of a bubble in house prices.



For the government to underwrite a huge piece of the credit-creation industry also raises broader questions. Why do it at all? And, if housing, why not business lending? Both Fannie and Freddie are publicly traded companies, and their shareholders, which have included Berkshire Hathaway, run by Warren Buffett, have benefited handsomely from their implicit government guarantees.

Answers to these questions take several forms. Perhaps housing loans should be subsidised, particularly for the poor, because home ownership is desirable. Even if true, this only partly gets Fannie and Freddie off the hook. For their ambitions focus ever more on moving upmarket. They are lobbying for the cap on mortgages that they can offer to rise, from $275,000 to $412,000—to help the "ill-housed wealthy", perhaps, murmurs one analyst? A recent study by the Congressional Budget Office provoked the agencies' fury by claiming that the advantages they enjoyed were far larger than had been thought, and that much of the benefit of the government subsidy went to shareholders rather than borrowers.

For their part, Fannie Mae and Freddie Mac argue that they are not really backed by the government, so they enjoy minimal competitive advantages. This claim is absurd. It also sits uneasily with their strategy of turning their debt into the main benchmark for fixed-income securities, replacing Treasury bonds, and with plans to sell their debt to retail investors as a low-risk investment.

There are big questions, too, about the quality of their lending and risk management. Congressman Richard Baker, a tireless critic of the two agencies, has wondered if they might not become the source of the next global financial crisis. Credit losses have been increasing, and the agencies' leverage is scary. According to calculations by a research firm, Graham Fisher, their debt-to-equity ratio ranges from 30 to as much as 84, depending on what assumptions are made about off-balance-sheet exposures. Further, new accounting standards that require fuller disclosure of derivatives losses raise fresh questions about the adequacy of the agencies' capital, never as large relative to loans as at the big retail banks. Declining capital adequacy may yet force the agencies to cut back their activities.

Mr Baker has been calling for a tough new regulator for Fannie and Freddie, under the auspices of the Fed. But at a hearing on July 11th, he changed tack, raising the possibility of licensing new home-loan agencies to compete with Fannie and Freddie. This idea, worth debating, seems to have come from high up in the Bush administration. It has attractions, not least that greater competition might force Fannie Mae and Freddie Mac to pass on more of their subsidy to consumers. On the other hand, after the government has spawned two mortgage monsters, is it wise to create any more?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The American economy

Greenspan's glimmer

Jul 19th 2001 | NEW YORK
From The Economist print edition

A turning point? Possibly

"WE ARE seeing signs that the bottom is beginning to structure itself." Hardly a cry from the rooftops, but then this was Alan Greenspan. In answers to questions after his half-yearly testimony to Congress on July 18th, the Fed chairman sounded in better spirits than during the set text of his speech. The economic outlook is "clearly far better, given what has happened, than I would have forecast six, eight, nine months ago," he continued. "We have come a long way through this adjustment process and we are still standing, which is good news as far as I'm concerned."

The evidence remains that the second-quarter GDP data, out on July 27th, will be dreadful. The economy may have shrunk. Yet Mr Greenspan has reason to believe that this may be close to the bottom. In recent weeks, some of the most reliable leading indicators of activity have stopped falling, and some have even started to turn up.

Two surveys by the National Association of Purchasing Managers (NAPM) rebounded in June, with services recovering even more strongly than manufacturing. The combined, weighted NAPM rose from 45.8 in May to 50.9 in June. The Chicago Purchasing Managers Index also rose sharply in June, to the highest since December. This suggests that manufacturers may see light at the end of the tunnel, even though industrial production has fallen for nine months in a row. On July 13th the University of Michigan index of consumer sentiment edged higher for a third consecutive month. And the growth in the money supply is outstripping nominal GDP growth by more than at any time since 1983, which may signal a rise in demand.

This may yet turn out to be a false dawn. As Mr Greenspan made clear, "downside" risks are still large, and more interest-rate cuts may be needed. Unemployment continues to rise, which could undermine consumer confidence. However, whatever happens to jobs, disposable income looks sure to grow for the rest of this year, thanks to tax cuts and lower mortgage rates. Another fall in share prices would have a big impact; certainly, lousy corporate profits make shares look overvalued. But, hey, it's summer—and some little tad of optimism may be in order.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

German finance

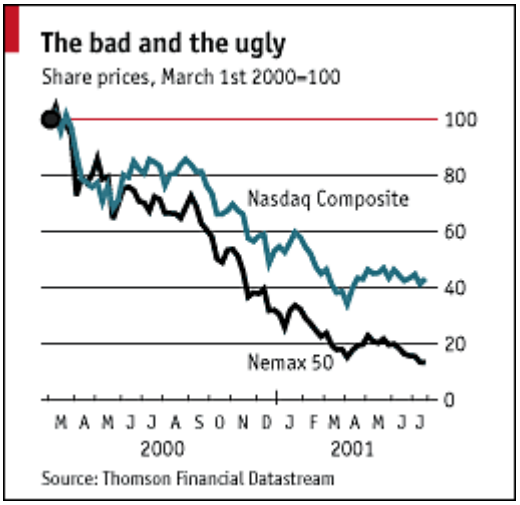
Penny bazaar

Jul 19th 2001 | FRANKFURT
From The Economist print edition

Frankfurt's high-tech stockmarket goes from bad to worse

QUITE often these days, German newspapers print lists of abysmal performers on the Neuer Markt, Frankfurt's market for so-called "growth" stocks. The challenge is to keep the lists short. Almost half of the firms in the supposedly top-notch Nemax 50 index have fallen by more than 90% from their peaks. The index itself has shed 88% since March 2000—more than tech markets in London or Paris, and far more than the Nasdaq in America, which has lost a mere 60% (see chart).

Worse, the Neuer Markt has been falling ever further behind its giant American cousin. In the second quarter of this year, when Nasdaq regained some lost ground, the Nemax 50 weakened again. This was the first time since the third quarter of 1999 that the two had moved in opposite directions. (For both, the third quarter of the year has begun poorly.)



The tech bubble inflated even more in Frankfurt than in New York: hence the bigger pop. The stars of the boom have fallen farthest in the bust—among them EM.TV, a media company, and Intershop, a software firm. Some managers also went beyond optimism in what they told investors about business prospects. Investigators are looking into several instances of questionable share dealings. And the bad news keeps on coming. This week, Management Data, a broadcasting-software company, said it had begun insolvency proceedings.

Add to all this Germans' lack of experience as shareholders (compared with Americans, in particular) and the result is a deep distrust of almost anything listed on the Neuer Markt. A few companies now say they might even consider moving to a more reputable corner of the Frankfurt exchange, or to London or New York.

Analysts are especially disparaging about "penny shares". About one-tenth of the market's 342 shares trade at less than *euro*1 (86 cents) apiece, including one in the Nemax 50 (its name: Fantastic). Half of the Nemax 50 companies have a market capitalisation of less than *euro*250m, scarcely blue-chip status. Critics want the wheat sorted from the chaff: they say that penny shares, which are prone to manipulation, should be delisted, with the Nemax 50 also shorn of, say, 20 members.

Deutsche Börse, which runs the tech exchange, has been trying to rebuild the Neuer Markt's reputation, by tightening regulations. Since March, companies have been obliged to report directors' share dealings; these are also listed on the market's portal for private investors. Now it is thinking about new measures, including delisting penny shares that remain below *euro*1 for an extended period.

This would not stop the drift by itself: time, and a stronger world economy, may be the only healers. It could help, though. It has often been said that the dramatic fall in the Neuer Markt has been no bad lesson for German investors. Stripping out feeble shares might further focus their minds—as well as those of a few company bosses.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

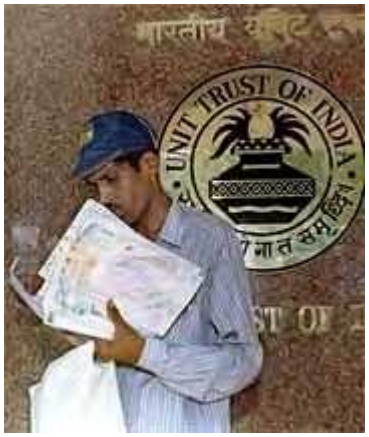
Indian mutual funds

Unit what?

Jul 19th 2001 | MUMBAI
From The Economist print edition

The government bails out its own fund, for the second time

FOR millions of investors, India's biggest and oldest manager of mutual funds, Unit Trust of India (UTI), has shed its middle name. On July 2nd its open-ended fund, US-64, with assets of 127 billion rupees ($2.7 billion), suspended sales and purchases of units—until January, it said—in a move prompted by falling share prices and the exit of some large investors.



Feeling diminished

The result: around 20m furious investors, with allegations of mismanagement hurled at the government, which controls UTI. The government promptly sacked UTI's chairman, Pavagada Subramanyam. And the finance minister, Yashwant Sinha, promised a partial rescue for small investors, the details of which were announced on July 15th.

Under the rescue plan, investors can sell up to 3,000 of their units to the fund, from August 1st. There is a government-supported floor price, which rises the longer investors stay with the fund. Otherwise, the government fears a crash, since the 37-year-old fund has holdings in many of Bombay's listed companies. UTI's new chairman, Meleveetil Damodaran, says the fund might sell shares privately rather than on the open market.

Persuading investors to stay in the fund will not be easy. Those who stayed after the previous government rescue, three years ago, have lost money. That rescue came after a government-appointed expert panel suggested that US-64 should be restructured as a bond fund; today, about two-thirds of its portfolio is still in shares. Another suggestion, that the fund should be regulated on a par with India's private funds, was ignored. Lack of regulation seems to have encouraged its managers to make risky investments.

US-64 failed to adapt to a changing market. Interest rates fell after financial deregulation in the mid-1990s, and the fund invested heavily in shares in an attempt to boost returns. Even as the market fell, the fund continued to quote unit prices above its net asset value. Many now fear another shock when it declares the market value of its assets next January.

The fund's rescue underscores the nature of the moral hazard that comes from the government's control of India's biggest financial institutions, including the banks and insurance companies. Most of India's household savings—around one-tenth of GDP—are locked into these inefficient and poorly managed institutions. Capital allocation and the economy suffer as a result.

The government has taken some steps to reduce its role. Privately managed mutual funds (unit trusts) have cut UTI's share of the market, from over 90% to 57% today. Several foreign insurers have set up shop this year. In March, Mr Sinha cut the fixed returns on government-managed pension funds. The next step should be to deregulate pension funds and let private managers run them. A smaller US-64 may, in the end, prove no bad thing.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Pampering staff

Elf help

Jul 19th 2001
From The Economist print edition

A Swiss bank finds a cure for British absenteeism

DISHWASHER not working? Your elderly relative needs driving to Oxford? When such challenges hit you during a working day, the extra stress can eat into your performance—and that of your employer. Step in the "concierge service".

A telephone call to such an outfit unleashes willing elves to call car companies or repair services, or to wait at home for you until the plumber, electrician or new Aga arrives. Concierge services are the rage among top American companies. Of *Fortune* magazine's 100 "best companies to work for", 29 list concierge services as part of their employee benefits.

Now UBS, a big Swiss-owned bank, is offering a "lifestyle-management" programme to its staff in Britain. The British government reckons that £10 billion ($14 billion) a year is lost through absenteeism, with every employee taking on average nearly four days a year off (without even being sick). UBS wants to reduce its own absenteeism by helping to take the stress out of its workers' home life.

Employees can choose a deal with a lifestyle-management company, Enviego, as part of their flexible benefits. A call to Enviego staff at any time of day or night helps them or their dependants to find a child-minder, medical or legal advice, theatre tickets or a dog-walker. (They still have to pay for each service, but not the £55 monthly subscription that Enviego charges private clients.) So far, the service does not extend to marriage guidance or, indeed, to stress-counselling for those who lose their jobs. And one thing firmly off the list is providing hostesses, says Enviego's managing director, Tom Shorten, once a trader at Deutsche Bank. ABN Amro, a Dutch bank, plans to offer concierge services to its British employees soon.

Does "lifestyle management" help? It may merely be a subtle way to keep noses to the grindstone for longer, says one cynic, causing more stress, not less. Waiting for the gas man can, indeed, be therapeutic. The Americans already have an answer to that, says Chris Ashford, head of human resources at UBS Asset Management: some enlightened companies allow their employees to take two wild-card "duvet days" a year. Is this the end of the British art of "doing a sickie"?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

French banking

Farmers unite

Jul 19th 2001 | PARIS
From The Economist print edition

Crédit Agricole is readying for an assault on Crédit Lyonnais, and beyond

"IT'S an elephant, but it's a smart elephant." So a former French Treasury official describes Crédit Agricole, a massive, slow-moving, mutually owned bank which, with capital of *euro*28 billion ($24 billion), is France's biggest and the sixth-largest in the world. For decades, Crédit Agricole has wondered what to do with itself. Should it remain true to its origins in rural France, or should it build a truly international business?

A flock in search of a listing vehicle

The bank seems to have made up its mind. It has just unveiled more details of a plan to list part of itself on the Paris bourse by the end of the year. It wants to use its new shares to pounce on Crédit Lyonnais, France's sixth-biggest bank, which is vulnerable after a shareholder pact designed to protect it from being taken over ended this month. Beyond that, the bank wants to expand in Europe, perhaps, by adding to its existing stakes in Banca Intesa in Italy and Banco Espirito Santo in Portugal.

Crédit Agricole is not the only French mutual bank bent on European expansion. When Caisse d'Epargne, another mutual, last month announced an alliance with Caisse des Dépôts et Consignations, a complex state-run financial group, it argued that mutual banks as well as publicly listed ones must play a role in European banking consolidation. Both Crédit Agricole and Caisse d'Epargne, in fact, worry that they could be left behind if their listed rivals, BNP Paribas and Société Générale, use their shares to deepen alliances and buy other banks in Europe. Mutual banks can only use cash for acquisitions, and most do not have enough of it to strike big deals.

The solution would be to demutualise, as building societies have done in Britain—except that French law forbids it. So the country's mutuals need a discreet way to shed their status in all but name. Crédit Agricole's plan for a listing vehicle is seen by French bankers as a first step towards what amounts to demutualisation.

For now, power in the group lies with nearly 50 regional banks, owned by over 2,000 local banks, which are, in turn, owned by 5.5m mutual stockholders. The regional banks own 90% of the central body of the bank, Caisse Nationale de Crédit Agricole (CNCA). CNCA owns the group's various subsidiaries or "factories", such as Crédit Agricole Indosuez and Crédit Agricole Asset Management.

Crédit Agricole's complex listing plan will mean that the regional bosses, or "barons", as they are known, will hand over some of their ownership of CNCA to outside shareholders, lowering the regionals' share to 70%. CNCA will also itself take a 25% stake in the regional banks. Crédit Agricole will retain its mutual character, since control stays with the regional banks. But if a merger with Crédit Lyonnais or other banks in Europe looks like happening, more power would shift from the regional banks to the CNCA. Eventually, Crédit Agricole would come to look like any other centrally run bank, owned by shareholders demanding a proper return.

France's two biggest listed banks, BNP Paribas and Société Générale, would welcome other mutual banks following Crédit Agricole's example. The transformation, they believe, would make the mutuals more interested in profits and less in maintaining market share. For years the publicly quoted banks have complained loudly about competitive distortions in the French banking system, and in particular about mutual banks' privileges. The Caisse d'Epargne and the French post office, for instance, share a

monopoly over the most popular tax-free savings account in France, the Livret A.

Although most people outside France usually think of BNP Paribas and Société Générale when it comes to retail banking in France, mutual banks in fact have three-fifths of the market. The biggest mutuals have used their decentralised ownership and grassroots presence to forge relationships with retail and small-business customers. And, though by and large they have also thrown off government control, they still have immense lobbying power, says Jean-Luc Lepreux, a banking analyst with Moody's in Paris. Their people in the regions know all the local "notables".

The mutuals have weaknesses, even so. If Caisse d'Epargne is to fulfil its wider ambitions, it needs to turn its new alliance with Caisse des Dépôts into something more than an uneasy peace between the two banks' heads, Charles Milhaud and Daniel Lebègue. The two men recently turned to a Canadian mediator to resolve their differences. For now the joint venture between the two is nicknamed in Paris a "usine à gaz"—gas-works—thanks to its complex and unwieldy structure.

Crédit Agricole's chief problem is its under-representation outside the poorer, rural regions of France. As it happens, Crédit Lyonnais would bring strength in Paris, Lyons and Marseilles. Buying Crédit Lyonnnais will not be easy, however, even though the mutual is the government's clear favourite for its 10% stake. Crédit Lyonnais's other main shareholders, among them Société Générale and Allianz, a German insurer, are unlikely to let the prize go to Crédit Agricole without a struggle, whatever the government's preference.

Besides, Crédit Agricole cannot make a conclusive move on Crédit Lyonnais until its own shares begin trading later this year, at the earliest. By then it may be too late. It took years for the regional barons to reach a unanimous decision about the listing, and some still mutter against it. Crédit Agricole could find itself divided over the issue of Crédit Lyonnais at the very moment when it needs to be single-minded about fighting off rival bidders.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economics focus

Frédéric Bastiat

Jul 19th 2001
From The Economist print edition

A 200-year-old's libertarian insights remain both relevant and amusing

IT IS not called the dismal science for nothing. Even the funniest jokes about economists usually elicit a titter, at best. If you laid all the economists in the world end to end, they still wouldn't reach a conclusion. There's no such thing as a one-handed economist: it's always on the one hand this, on the other hand that. And so, excruciatingly, on.

A little better are the jokes that economists tell to other economists. One of the best is about the two believers in efficient-market theory out walking together. "Isn't that a $10 bill?" says one. "Obviously not," says the other. "If it were, somebody would have picked it up." A website devoted to economics jokes is a godsend for economists wishing to inject a lighter note into their lectures.

Rare indeed are economists who use humour to communicate their theories. In the history of economic thought, Frédéric Bastiat, born 200 years ago, stands out as a beacon of light-heartedness, thanks to his brilliant use of satire. Better still, his wit was deployed in defence of liberty and free trade, causes dear to *The Economist*'s heart. Shortly after this newspaper was launched in 1843 to campaign against Britain's protectionist Corn Laws, Bastiat wrote, in all seriousness: "May all the nations soon throw down the barriers which separate them. One of the most efficacious means of attaining this great result would be the propagation of the Journal entitled the 'ECONOMIST'."

Unfair competition

Bastiat is best known for an essay* in which he petitions parliament on behalf of the candle makers of France. His complaint is against the "ruinous competition of a foreign rival who works under conditions so far superior to our own for production of light that he is flooding the domestic market with it at an incredibly low price." The rival is the sun. His proposed remedy is the mandatory shuttering of all windows. That, he claims, using all the standard protectionist arguments, will benefit not only the candle industry but also all the industries that supply it. As a compelling statement of the case for free trade, this essay is hard to beat.

During the building of a railway to Paris, it was proposed that there should be a break in the line at Bordeaux because it would help businesses there, such as porters, storage firms and hoteliers. Brilliant, said Bastiat. What better way to boost prosperity in France than to have similar breaks at Angoulême, Poitiers and all intermediate points? "By this means, we shall end by having a railroad composed of a whole series of breaks in the tracks, ie, a negative railroad."

Noting the popular view that exports are good and imports bad, Bastiat wondered if the best outcome would be for ships carrying goods between countries to sink, thus creating exports without imports. Debunking the "lump of labour fallacy" before it was even given that label, he suggested that to parcel out the limited amount of work available, people should be required to use only one hand, or even to have a hand chopped off. Missing the irony, France recently imposed a maximum working week of 35 hours a person, hoping to share out available work.

Bastiat also delivered witty one-liners: the state, he said, "is the great fictitious entity by which everyone seeks to live at the expense of everyone else." He was an early critic of socialism. In "The Law", a sombre work published shortly before his death in 1850, he described how the state, by identifying with the interests of producers rather than consumers, often came to commit "legal plunder". The main role of the state, he argued, should be to protect property and liberty.

Whether Bastiat was a great economist or merely a great communicator of economic truths has been much debated. Joseph Schumpeter had his doubts, calling him merely the “most brilliant economic journalist who ever lived.” Ludwig von Mises was kinder, saying that “his critique of all protectionist and related tendencies is even today unsurpassed.”

Certainly, in “What is seen and what is not seen”, Bastiat asserted the importance of taking into account “opportunity cost”, one of the great insights of economics, long before anybody came up with the jargon. Noting how people often see a silver lining in a bad event, such as a broken window being good for the glazier, he showed how the money paid to repair the window would now be unavailable to spend on other goods, causing the workers who make them to suffer. Thus the destruction of the window was bad for the economy as a whole.

His work remains timely, especially with protectionist tendencies on the rise. France should certainly pay heed to its largely forgotten son. Last month, a ceremony marking Bastiat’s bicentenary in his hometown of Mugron, attended by foreign economists, was disrupted by anti-globalisation protesters. A planned visit to the vineyards of Minervois was cancelled because of violent protests by wine-growers demanding subsidies to compensate them for lower prices due to competition from imported wine. Bastiat would have found this fertile ground for an entertaining pamphlet. Yet perhaps the flourishing of such economic illiteracy more than 150 years after his death is no laughing matter.

---

*English translations of most of Bastiat’s works are available from the Foundation for Economic Education, Irvington, New York.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Climate change

Kyoto's last stand

Jul 19th 2001
From The Economist print edition

The future of the global climate-change treaty looks bleak. The negotiations in Bonn are unlikely to change that

Get article background

WHAT is at stake in Bonn? That is the question hanging over the current gathering in Germany's former capital of the world's environment ministers. The answer ranges from everything to nothing, depending on whom you ask.

Officially, ministers are meeting in Bonn to work out the final details of the Kyoto Protocol. That UN treaty, if ratified, would bind industrialised countries to cut their emissions of greenhouse gases significantly over the next decade. Such gases, most notably carbon dioxide, keep the earth warm by slowing the radiation of heat into space. A recent increase in their quantity is, however, causing the planet's surface temperature to rise, which may have adverse climatic consequences.

Ask many environmentalists, and they will say that the planet's very future is at stake at Bonn. They will point to mounting evidence that climate change is real, and insist there is not a moment to lose. The publication earlier this month of the final report of the UN's Inter-governmental Panel on Climate Change lends weight to their position. The report's most dramatic conclusion, heavily trailed beforehand, is that the range of warming over the next century is likely to be between 1.4°C and 5.8°C. This doubles the upper bound of the IPCC's previous estimate.

Ask the Americans (or, at least, the American delegation), and you will get the opposite response: nothing much is at stake in Bonn. The American administration considers the pact "fatally flawed", and will not change its mind in any circumstances, according to Paula Dobriansky, the head of that delegation. She will turn up in Bonn merely to ensure that "American interests" are not trampled on by overzealous Europeans.

Those Europeans have pitched their tents in the same camp as the greens. They reckon that the Kyoto Protocol, though imperfect, is the only game in town. On July 17th, the EU issued a declaration proclaiming that "climate change is taking place now. Its consequences will be felt globally. Time is pressing and the international community cannot afford to postpone action." Jürgen Trittin, Germany's environment minister, goes further. Referring to America, he said that "we cannot allow the country with the biggest emissions of greenhouse gases to escape responsibility for protecting the global climate."

Even before the inauguration of George Bush in January, Europe and America did not exactly see eye to eye over what should happen. Last November, negotiators met in The Hague to try to iron out their differences. The Americans, then represented by the Clinton administration, insisted on a reinterpretation of the Kyoto treaty. They wanted to allow the liberal use of "carbon sinks", such as new forests, to absorb carbon dioxide from the atmosphere by converting it into plants. They also wanted unfettered emissions trading (buying the right to emit greenhouse gases from places that would find applying controls cheaper than did the purchaser).

That was hardly an outrageous request, for it would have made tackling climate change as flexible and inexpensive as possible. It would also have made the treaty more palatable to a hostile American Senate.

EU ministers nevertheless rejected it, striking a moralistic note by insisting on sharp limits to such flexibility. The meeting broke up in disarray.

The parties agreed to continue their negotiations at this week's Bonn jamboree. But now Europe has to deal with an even more sceptical American administration. In March, Mr Bush reaffirmed his campaign pledge to reject the Kyoto treaty outright. When they realised they could not persuade him to change his mind, the Europeans vowed to forge ahead anyway. Unfortunately for them, the treaty cannot come into force unless it is ratified by 55 countries making up the source of at least 55% of the greenhouse-gas emissions of the rich world. Europe, with all the allies it can muster, cannot quite leap that hurdle. The crucial vote lies with Japan.

Tokyo v Kyoto

The early betting was that the Japanese could not bear the shame of seeing a global environmental treaty forged in their country's ancient capital go down in flames. However, while some parts of the Japanese establishment do want to stand by the EU, it now appears that a group of pragmatists, led by Junichiro Koizumi, the new prime minister, is gaining the upper hand. This crowd is wary of alienating America, which is Japan's strongest ally and chief trading partner. What is more, Mr Bush's men have been arm-twisting Japan to distance itself from the pact.

That has outraged the Europeans still further. They claim that Mr Bush had explicitly promised them, when they met at a recent summit in Sweden, that he would not pressure other countries to join him. To woo back the fickle Japanese, the Europeans have now moderated their hard line on carbon sinks, which the Japanese have indicated are of particular importance to them. Ironically, though, the EU softening on sinks comes just as a new report by the Royal Society, one of Britain's most venerable scientific institutions, argues against relying on them too heavily. The society's panel of experts reckons that too little is known about how sinks behave.

All in all, it is hard to see how the Kyoto treaty can be saved at Bonn. The only way would be if the Japanese suddenly swung to Europe's side. There is a slim chance this might happen: heads of government of the rich and powerful G8 meet in Genoa, Italy, this weekend, and the group's European members plan to ambush Mr Bush and Mr Koizumi on the matter.

But on balance, a *volte face* seems unlikely: Japanese governments tend to put off hard decisions for as long as possible. The likelier outcome is that the Bonn meeting will prove inconclusive, and that Kyoto will limp along until negotiators meet yet again, in Marrakech in October. It would almost be kinder to kill it off now.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Hydrogen-powered cars

Replacing gas with a gas

Jul 19th 2001
From The Economist print edition

BMW wants to make internal-combustion engines that run on hydrogen

ONE way that global warming might be reduced is by powering cars with something that does not release carbon dioxide when it is burned. That is part of the idea behind a "hydrogen economy"—a future in which hydrogen, which can be produced from renewable sources, takes over from hydrocarbons as the world's principal fuel.

Given this possibility (and also given the more immediately pressing need to produce vehicles that can comply with the exacting emissions standards of California), several of the world's car makers—notably Ford, DaimlerChrysler and Honda—are studying fuel cells. These react hydrogen and oxygen together in a controlled process, extracting energy in the form of electricity. Fuel cells, which are an old technology, certainly work, but they are still some years from commercial viability in cars. There is, however, an alternative: burn the hydrogen in a conventional internal-combustion engine. And that is what BMW proposes to do. This week it unveiled a prototype version of its 7-Series saloon car that has a hydrogen-powered engine.

Converting an engine to run on hydrogen is relatively simple. It requires a bit of new plumbing and a few extra lines of code for the engine's control computer. With a little jiggling, the motor can be made "dual-fuel", so that it can still run on petrol as well. That would allow the infrastructure of a hydrogen-delivery network to be introduced gradually, rather than being put in place more-or-less instantly.

Given the ease of conversion, and the possibility of a piecemeal transition to a full-scale hydrogen economy, this would seem the logical way to proceed. There are, however, two catches. The first is that fuel cells are a far more efficient way to use hydrogen than burning it. When the sums are done, a fuel-cell-powered vehicle would manage 60% more kilometres per litre than a hydrogen-powered internal-combustion engine. The second is that, gram for gram, hydrogen contains significantly less energy than petrol. Performance will reflect that, unless those clever engineers at BMW can somehow overcome the difference. If they cannot, then BMW, whose prestige and independence rely largely on its engine-making ability, may be in trouble. Were fuel cells to become the standard, the firm's future could be bleak.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

The origins of malaria

Following the plough

Jul 19th 2001
From The Economist print edition

A genetic study suggests that malaria may have evolved because of farming

Get article background

AIDS tends to hog the headlines, but several other infectious diseases still stalk the tropics, killing and debilitating those who catch them. As with AIDS, the origins of these diseases are not merely of academic interest. Knowing how they first spread to people may help to stop the same thing happening again.

Two papers published recently in *Science* have helped to pinpoint the origin of malaria—the most lethal tropical infection until AIDS came on the scene, and a disease that still infects 200m-300m people a year, killing over 1m of them. According to work published this week by Sarah Volkman, of Harvard University, and her colleagues, *Plasmodium falciparum*, the parasite that causes the severest form of malaria, seems to have got going between 7,700 and 3,200 years ago. A study published in June, by Sarah Tishkoff of the University of Maryland and her colleagues, comes up with a range of 11,760 to 3,840 years ago.

Both teams looked at gene frequencies to arrive at these estimates. Dr Volkman studied the genes of the parasite itself. Dr Tishkoff examined those of its host, *Homo sapiens*. Both were testing a hypothesis first proposed in 1958 by an anthropologist called Frank Livingstone.

Dr Livingstone thought that the emergence of malaria might have been connected with the beginning of agriculture. He argued that sunlit pools left in patches of forest cleared for farming would have been perfect sites for the mosquitoes that transmit the disease to breed in, and also that the growing human populations that agriculture permitted would have provided an abundance of convenient hosts.

Dr Volkman and her team tested this idea by looking at the range of genetic variation found in *P. falciparum*. In general, the more variation there is in a gene in a population, the longer it is since that population's individuals shared an ancestor. Such variation can therefore act as a "molecular clock", from which the age of the common ancestral gene can be deduced.

The best genes for this purpose are so-called neutral genes: those that are not subject to strong selective pressures that will stop random mutations from accumulating them. Averaged over a sufficient period, such random changes accumulate at a constant rate in neutral genes. But previous studies of genetic variation in *P. falciparum* have concentrated on those genes that help the parasite to evade the human immune system, or protect it from insecticides. These are clearly subject to strong selective pressures, and therefore make poor molecular clocks.

When Dr Volkman looked at nine neutral genes, she found little variation across widely separated parasite populations, suggesting the common ancestors of those genes were recent. And when she applied estimates of the speed of mutation to her results, the ages coincided neatly with the Neolithic agricultural revolution.

Dr Tishkoff and her colleagues studied the frequency of variants in the human G6PD (glucose-6-phosphate-dehydrogenase) gene, which confers resistance to malaria. G6PD carries the instructions for making an enzyme that is essential for the transport of oxygen in the bloodstream. Mutations in this gene may have adverse consequences for a person's health but, rather like the mutation of the haemoglobin gene that causes sickle-cell anaemia, they can also protect that individual against malaria.

Again like the sickle-cell gene, some G6PD mutations have spread in parts of the world in which malaria

is endemic. Dr Tishkoff reconstructed the recent history of G6PD by examining the variants present in more than 450 Africans. She then simulated the way that the mutations spread to find out how long the process took. And, just as Dr Volkman did, she hit the Neolithic.

How much light all this sheds on the risks of new infections is unclear. But there is a respectable argument that the cutting of tropical forests for farmland and timber, by bringing people into close proximity with wild animals that they would not previously have encountered, may encourage the spread of new diseases. Perhaps things have not changed so much in the past few thousand years, after all.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Bacteria and ore-formation

Goldbugs

Jul 19th 2001
From The Economist print edition

Gold mines may owe their origins to microbes

MEDIEVAL alchemists found, in the end, that they could not create gold. Modern geochemists have a similar problem. They find it hard to understand how natural gold deposits form. There is much handwaving about gold-rich fluids from deep in the earth, and chemical precipitation, but the physics does not add up. The answer may be that what is happening is not geochemical at all, but biochemical. And a casual experiment by a bacteriologist may hold the key.

Derek Lovley, of the University of Massachusetts, Amherst, has been studying "metal-eating" bacteria for two decades. These bacteria make their living by converting (or "reducing") the dissolved ions of metallic elements from one electrical state to another. This reduction releases energy, which the bacteria extract for their own purposes.

Unsurprisingly, such bacteria tend to prefer common metals such as iron and manganese for lunch, though some species are able to subsist on such exotica as uranium. A few months ago, though, as "a bit of a lark", Dr Lovley decided to put some of his bacteria into a solution of gold chloride. He was fully prepared for nothing to happen, as gold compounds are generally toxic to bacteria. Instead, the test tube containing the solution turned a beautiful shade of purple, the colour of metallic gold when it is dispersed very finely in water.

Bacteria are already known to be involved in the formation of an iron ore called limonite, and Dr Lovley has argued that they are also involved in the creation of certain ores of uranium. His jokey experiment, reported in the July issue of *Applied and Environmental Microbiology*, opens up the possibility that gold deposits, too, may have a bacterial origin, with the microbes acting as the agent that concentrates gold from sources such as volcanic springs into a form that people can mine.

Dr Lovley has some support among geologists. According to Francis Chapelle, of the US Geological Survey's branch in South Carolina, his hypothesis would neatly explain the origin of some of that state's gold deposits. The rocks of the Carolina slate belt, including the Haile gold mine, contain the metal in an unusual form: rather than appearing in veins and nuggets, it is finely disseminated in a layer of sedimentary rock.

The sediments that form the Carolina slates were once a seabed through which volcanic fluids flowed. According to Dr Chapelle, metal-reducing micro-organisms may have extracted gold ions from these fluids, reduced them, and dropped the waste (ie, metallic gold) as a powdery precipitate in the sediments. How that relates to the more traditional deposits of gold in veins and nuggets remains to be seen, although the fact that several species of Dr Lovley's gold-eating bacteria prefer high temperatures suggests they might survive well in the hot environments mineral veins are thought to form in.

Dr Chapelle also suspects that Dr Lovley's discovery may have a bearing on the origin of the vast Witwatersrand goldfield in South Africa, whose mines produce about one-third of the world's supply. Like South Carolina, Witwatersrand has an area of gold that is found not in igneous rocks but in a thin sheet, sandwiched among sediments. Perhaps the Boer war was actually triggered by arguments over bacterial excreta.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Air travel

The way we fly now

Jul 19th 2001
From The Economist print edition

Airship splendour for an elite, pictured below, has long since given way to airline misery for the masses. A new book proposes a remarkable solution

Mary Evans

Free Flight: From Airline Hell to a New Age of Travel
By James Fallows

PublicAffairs; 272 pages; $25. Plymbridge; £17.99

Buy it at
Amazon.com
Amazon.co.uk

"HOW can a system be so technically advanced and admirable, yet lead to results so unpleasant for everyone?" wonders James Fallows in this delightful book. The system is air travel. When all goes well, you marvel at the speed and reliability of the technology. But often, all does not go well. You drive for miles to the airport, you queue for ages, you wait forever in the departure lounge. For this misery, Mr Fallows thinks there is a cure.

He is admirably qualified to describe it: he is not just a top journalist but also an amateur pilot, and his book is built around a heart-stopping description of a flight across America with his wife and son. "Free Flight" makes some fascinating detours along the way. It describes, for example, the travails of setting up a new business (Cirrus, a family firm in Minnesota that makes small aeroplanes). And it lucidly explains the reason why pilots of small aeroplanes understand that they are riskier than big ones yet accept the risks, believing that most can be controlled.

Flying across America in a private plane is a joy; a journey on a commercial airline can become a nightmare. Door-to-door, a flight of 500 miles or less (the majority of American flights) is no faster than driving a car. Why? Because, Mr Fallows argues, of the hub-and-spoke system, developed by the airlines since deregulation to cut their costs and fill their seats. More than 80% of America's airline travel now takes off from or lands at the busiest 1% of airports. Air traffic has grown roughly twice as fast as the economy for years—but traffic concentrated on these hubs has grown much faster. Thus in the 20 years to 1998, the annual total of take-offs and landings at Cincinnati soared from 76,000 to 367,000. At the same time, the big carriers sharply cut the number of cities they serve, from 463 in 1978 to 268 two decades later. Smaller "spoke" airlines scoop up passengers at the hubs and distribute them to their final destinations.

Hubs make the whole system more cumbersome and vulnerable to delays. When a problem hits a big hub, it ripples out through the network. The answer, says Mr Fallows, is one that NASA, America's space agency, has been looking at: many more flights by small aircraft into the myriad airports scattered across the country. More than 98% of the American population lives within a 30-minute drive of one of 5,000 public-use landing facilities. With suitable safety investment, NASA reckons these could support 500m take-offs and landings a year, instead of the present 37m.

But that requires a revolution in aeroplane design, and most of Mr Fallows's book is about two companies

leading it. One is Cirrus, which makes simple little aeroplanes, aiming for the airborne equivalent of a modern car—with the unique safety feature of a parachute for the entire aircraft. The other, Eclipse Aviation in Albuquerque, is working on a project to build a small jet costing less than $1m and designed to land on runways only 2,500 feet (769 metres) long.

Aircraft design has not changed fundamentally in decades. Designers of small aircraft, in particular, concentrated on the corporate jet market. Now, says Mr Fallows, these companies are aiming at a new market—air-taxis and even amateur pilots such as himself. As small aircraft become simpler to fly, so a new market will emerge for direct flights between local airports. If costs continue to fall and safety standards continue to rise, the true promise of air travel would arrive: ordinary people would enjoy a high degree of flexibility and convenience that, until now, has been available only to the rich. There would then, at last, be an automobile of the sky. Far-fetched? Perhaps. But so, once, was cheap air travel.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

A philosopher's letters

Love, Bertie

Jul 19th 2001
From The Economist print edition

"A GREAT deal of work has come upon me, neglect of some of which might jeopardise the continuation of the human race," wrote Bertrand Russell in a letter in 1967, explaining why he did not have time to comment in detail on a philosophical manuscript. Few dons could carry off such an excuse. Russell was, in his final decade, concentrating on three large campaigns: helping Soviet Jews, opposing the Vietnam war and crusading for nuclear disarmament. The excuse might at first seem to be evidence of lunatic self-importance, or maybe senility (he was 95 at the time). But those who knew him would recognise its characteristic mix of a melodramatic, gently ironic style together with a profound commitment to public benevolence and political action. Activism ran in the family. A 17th-century ancestor was executed for his part in a plot to assassinate Charles II, and Russell's grandfather introduced the first reform bill and was twice prime minister.

The Selected Letters of Bertrand Russell: The Public Years, 1914-1970
Edited by Nicholas Griffin

Routledge; 680 pages; $35 and £25

Buy it at
Amazon.com
Amazon.co.uk

Anybody who reads this splendid and revealing selection of letters will soon feel that he knows Russell—though not, of course, as well as its editor, Nicholas Griffin, does. Mr Griffin is director of the Bertrand Russell Research Centre at McMaster University in Hamilton, Ontario, which has over 40,000 letters by Russell—estimated at between a quarter and a half of the total number he wrote—and is also editor of Russell's "Collected Papers", of which 14 volumes have been published so far, with another 17 or so to come. "When I am out I see such millions of people, and do so much altogether—no one has the least idea how much I get into a day," Russell wrote from prison to Lady Ottoline Morrell in 1918, bemoaning the fact that he would have less time for long letters when he was released from his sentence for pacifist activities. Mr Griffin, for one, knows all too well what Russell packed into a day.

With this volume of 388 letters covering the years 1914-70, Mr Griffin completes a two-volume epistolary biography unrivalled for its scholarship in the over-populated world of Russell studies. He adds linking commentary between the letters that would amount to a book in itself, and which clarifies many points, small and large, about Russell's eventful and controversial life. He scotches, for example, the often repeated claim that Russell once advocated a pre-emptive nuclear strike against the Soviet Union. Mr Griffin also provides copious and often pleasingly discursive footnotes to identify the allusions and people in the letters. There is plenty of incidental knowledge to be gleaned from these—concerning, for example, the Utraquist doctrine of the Eucharist, which makes an appearance in a hilarious reply to a spoof agony aunt letter that Russell received from a colleague at the school he founded after he had published his popular tract on "Marriage and Morals" and was being deluged with requests for sex advice.

The selection includes relatively few replies to letters from members of the public—always a large part of Russell's mailbag. Faced with an appalling task of sifting, Mr Griffin has chosen to focus on a handful of topics and follow them through, rather than provide a sample that is even-handedly representative of Russell's interests, which, Mr Griffin notes, included "everything under the sun, and a good deal else besides". Few of the letters he has picked have been previously published.

What comes across most powerfully from this selection is Russell's passion, his benevolence, and—perhaps most welcome—his humour. "I went all over southern California debating with a rabbi on the question 'Is monogamy doomed?' He argued in favour of monogamy, in the hope of getting enough money to leave his wife," Russell writes, describing a lecture tour to Lady Ottoline. To which Mr Griffin typically adds a wry footnote: "Newspaper reports from California reveal that Russell debated this topic with two rabbis—fortunately, we do not know which one is referred to here."

Bertie and the bomb

The following letters to the editor have been published in The Economist:

SIR – Your review of “The Selected Letters of Bertrand Russell” (“Love, Bertie ”, July 21st) states that the book's editor, Nicholas Griffin, “scotches, for example, the often repeated claim that Russell once advocated a pre-emptive nuclear strike against the Soviet Union. ” Let me unscotch it. I was in the audience at the public meeting at which Russell advocated precisely this, and it made a big impression on me at the time. The occasion was a gathering organised by some peace-loving foundation whose name I forget (my records are in store at present), held in 1948 or thereabouts, in the still roofless hall of Westminster School, of which I was then a pupil. When, some 20 years later, I recalled the event in the Spectator, which I then edited, I received (and published) a letter from the man who had organised the meeting. He corroborated my account and added how surprised and shocked he had been at Russell's proposal.

Needless to say, Russell advocated a pre-emptive nuclear strike on strictly humanitarian grounds. In a nutshell, he pointed out that at the time the Soviet Union did not yet possess a nuclear capability but that it would very soon do so, after which all history made it clear that sooner or later there would be a nuclear war between the two superpowers that would be infinitely more devastating than either of the two world wars through which he had lived. The only sure way of preventing this Armageddon, he concluded with remorseless if unpalatable logic, was for America to launch a nuclear attack on the Soviet Union before it acquired the bomb: after that it would be too late.

Lord Lawson, London

SIR – Lord Lawson (Letters, August 4th) is not alone in believing that Bertrand Russell advocated a pre-emptive strike against the Soviet Union in his 1948 speech at Westminster School: the Daily Worker headlined its report “Earl Russell calls for atom war.” Russell himself denied this interpretation in letters to the press immediately after the talk and was apt to blame a communist reporter in the audience for putting the story about for political ends. A transcript of the talk reveals that what he advocated was not a pre-emptive strike but “the line of policy which the western nations are now pursuing”, namely, “to make it obvious to the Russians that they can't make war successfully.”

The real trouble, however, came in reply to a question about the fate of Britain in a nuclear war. Russell said there were three alternatives, “*if the present aggressive Russian policy was persisted in*”, (emphasis in the original) “:(a) war with Russia before she has the atomic bombs, ending fairly swiftly and inevitably in a western victory; (b) war with Russia after she has the atomic bombs, ending again in western victory, but after frightful carnage, destruction, and suffering; (c) submission. ” He made it clear that he regarded each alternative as more catastrophic than the one before. But he did not advocate immediate nuclear war with Russia, because he obviously hoped that “the line of policy” which the western nations were pursuing would deter “the present aggressive Russian policy.” I cannot say I approve of the policy Russell did advocate on this occasion, but (press reports to the contrary notwithstanding) it clearly fell short of a pre-emptive nuclear strike. All the relevant texts will eventually be published in “The Collected Papers of Bertrand Russell”.

Nicholas Griffin, McMaster University,

Hamilton, Canada

SIR – We are getting there. Nicholas Griffin (Letters, August 11th) now concedes that, at his 1948 meeting at Westminster School, Bertrand Russell advocated an early pre-emptive strike against the Soviet Union, before the Russians acquired their own atomic bomb. But he adds that Russell made it clear that this drastic action should take place “if the present aggressive Russian policy was persisted in.” Mr Griffin insists, however, that Russell “obviously hoped” that this policy would not be persisted in. What in fact was “obvious”—and one of Russell's chief characteristics was his clarity—was that he expected that it would be, and was clear that we could not simply wait and see, as this would give the Russians time to acquire their own atomic bomb.

I was there when Russell spoke: Mr Griffin was not.

Lord Lawson, London

SIR – I certainly do not concede that Bertrand Russell advocated “an early pre-emptive strike against the Soviet Union”, as Lord Lawson claims (Letters, August 18th). What he advocated was a continuation of the West's policy of containment from a position of strength. In answer to a question as to what would

happen in the event that the policy failed, Russell said that a war before Russia had nuclear weapons would be less disastrous than one after she had them—he did not infer from this that a war should be started straightaway. The policy of containment was, of course, backed by the threat of war, but Russell's clarity of thought (which Lord Lawson praises) enabled him to see that this was quite different from advocating a pre-emptive strike.

Lord Lawson may have been present when Russell spoke but I have a verbatim transcript of what he said.

Nicholas Griffin McMaster University

Hamilton, Canada

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Summer movies

Hothouse flowers

Jul 19th 2001
From The Economist print edition

Many of this summer's blockbusters were rushed to release, and it shows

SUMMER, when it's hot outside but the cinemas are cool, is normally Hollywood's peak season. This year might be an exception. Though the writers' strike that threatened to close down production from early May was headed off at the gulch, nobody knew till the last moment that it would be averted. As a precaution, the studios have been rushing to wrap up movies, so that there would be enough product to keep everyone happy for many months into the expected shutdown.

But speed has a price. Movies that might have benefited from post-production tinkering have been hurried to completion. The results are starting to show. Summer has kicked off with two bona fide box-office hits, "Pearl Harbor" and "Shrek", both made at leisure, but several of the latest movies to open look as though they were too hastily prepared for release.

Ivan Reitman's sci-fi spoof, "Evolution", is an example. A tall tale of alien life forms drifting to earth and evolving into anything from flying cockroaches to pooches like miniature Jabba the Hutts, it trades wit for toilet humour and winds up with an outrageous example of product placement. "Evolution" feels scrappy and in need of pruning. Audiences responded accordingly, with a sluggish opening weekend take of only $13.4m from more that 2,600 screens. Disney's usually bankable summer cartoon—this year it's "Atlantis: The Lost Empire"—has been trounced at the box office by DreamWorks' "Shrek". An animatronic film, "Cats and Dogs", is also doing brisk business, with an original take on man's relations with his favourite pets: dogs alone can save us from feline evil.

If only on account of all the hype and anticipation, Steven Spielberg's "AI" and Simon West's "Lara Croft: Tomb Raider", in which Angelina Jolie plays a computer-game heroine, had fairly strong opening weekends; Tim Burton's remake of "Planet of the Apes" also looks set for an initial box office landslide. But after the first weekend it will be on its own.

A big question mark hovers over "Jurassic Park III". Without Mr Spielberg in the director's chair, and with no really top-flight stars to speak of, it will have to pull something very scary out of the hat to persuade audiences they haven't seen it all before. If critics rave about the film, that might be another story, but in this corner-cutting, beat-the-strike-deadline summer, the portents are not good.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Archaeology

Digging for truth

Jul 19th 2001
From The Economist print edition

ARCHAEOLOGY can seriously damage your health. If you're working in a politically sensitive country, it can kill you. It establishes history, and the past is a powerful weapon in present disputes over rights and claims. No one understood this better than Albert Glock, an American archaeologist who was director of the W.F. Albright Institute in Jerusalem from 1978 to 1980, and then of the Palestinian Institute of Archaeology at Birzeit University on the West Bank until 1992. Until January 19th 1992, that is, when he was ambushed by an unidentified gunman and shot dead at close range.

Palestine Twilight: The Murder of Dr Albert Glock and the Archaeology of the Holy Land
By Edward Fox

HarperCollins; 277 pages; £19.99. To be published in America as â€œSacred Geographyâ€ ; Henry Holt (October)

Buy it at
Amazon.co.uk

Glock came from a strict Lutheran background. He had originally travelled to the Holy Land, like so many Christian scholars and archaeologists before him, in order to "prove" the literal truth of the Bible. Over the years he had made the intellectual journey towards scientific scepticism, away from Christian fundamentalism—away, too, from the specifically biblical archaeology that goes with it.

By an ironic twist, this biblical archaeology serves the Israelis too, appearing to justify their claim to Israel. Anything later than the first century AD and you're on your way to Byzantium, the Ottoman Empire, Islam—and Palestine. Glock went all the way into enemy territory, as it were, and dedicated himself to an archaeology that would deliver history back to the Palestinians. But there were reasons why he alienated Palestinians as well as Israelis.

On one level, "Palestine Twilight" is a detective story of the hunt for Glock's killer. But, as Edward Fox says himself, understanding his murder means understanding a whole society. All through the book, the *intifada* mounts and, with it, Israeli searches, curfews, arrests, interrogations and torture. With the Gulf war the screws are tightened; to young Palestinian radicals, the Oslo talks feel like betrayal.

Glock, unlike most foreign nationals, remained at his post as things worsened. Against a background of fear, paranoia and xenophobia, he blocked the promotion of a Palestinian archaeologist, on the grounds of academic mediocrity. As stubborn and high-minded as his Lutheran forebears, he would not accept that, by then, everything had become political.

At which point, an ambush and a bullet seem plausible. But Mr Fox keeps his cool. There are other possibilities—shadowy paths that lead him farther afield, to Palestinian money in America, to Israeli prisons and the world of Palestinian collaborators, to Gaza and Hamas, the Islamic faction of the Palestinian resistance. By the end, Glock has become a small cog in a big machine. Or rather, a small key to a big door. Mr Fox brilliantly manages these questions of scale and perspective. His sense of drama and suspense—even of tragic destiny—keeps Glock at the centre of the story; and yet at the same time, anyone wanting to understand the trauma of occupied Palestine, historically, culturally and politically, should read this book.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Simone Weil and Rosa Parks

Two kinds of heroism

Jul 19th 2001
From The Economist print edition

WHAT unites these two very different women is their extraordinary personal courage in standing up to oppression and injustice—even though, as these excellent brief lives make clear, that courage itself took strikingly different forms. Simone Weil starved herself to death in exile out of solidarity for compatriots in German-occupied France. Rosa Parks, in December 1955 on a bus home from work in Montgomery, Alabama, was too tired to give up her seat to a white man. Her arrest touched off a 381-day boycott of the city's segregated buses, a landmark in the American struggle for civil rights.

Weil, a social thinker and religious mystic, is remembered as a heroine of the French resistance. Mrs Parks, now in her 80s, is commonly thought of as a humble seamstress, a black Everywoman. Weil's reputation corresponds to the facts; Mrs Parks's results from tactical distortion. Civil-rights activists played down her considerable political experience and sophistication—they needed a simple soul with sore feet in order to make the most of an incident on a Montgomery bus.

Mrs Parks was a member of the National Association for the Advancement of Colored People (NAACP) who had helped lead black voter-registration drives in Alabama, then a white-supremacist southern state. Her act of defiance on the bus was spontaneous, but, as Douglas Brinkley shows, she had been coached to play a significant part in the civil-rights struggle. Sponsored by a liberal white couple, she had enrolled in a training workshop on "radical desegregation" at the Highlander Folk School in Monteagle, Tennessee, where former pupils included Martin Luther King. Its founder and head, Myles Horton, had studied under one of America's most influential Christian thinkers, Reinhold Niebuhr, and was a promoter of the "social gospel". It was Horton's wife, Zilphia, who, along with two troubadours, Guy Carawan and Pete Seeger, made the hymn "We Shall Overcome" the anthem of King's Southern Christian Leadership Conference.

Mrs Parks was in her element at Highlander, for religion was, and remains, just as central to her life as it was to Simone Weil's, though she comes out of a different tradition. She is a steadfast member of the African Methodist Episcopal Church, a radical denomination which became known as "the Freedom Church" during the pre-civil war campaign to abolish slavery. Weil, the daughter of Jewish parents, was too much a religious free-thinker to commit herself to a particular denomination. She teetered on the brink of conversion to Catholicism but could never quite make the jump. Francine du Plessix Gray notes how Weil, during a spell in New York, went to mass each weekday at a Catholic church but at weekends attended a Baptist church in Harlem and a small synagogue of Ethiopian Jews.

Both in the central tenets of their politics and their faith, the two women nonetheless came to similar conclusions. They both resorted to passive means of protest to make their point, though neither ruled out the use of force if necessary. Once Germany invaded France, Weil was filled with remorse for her pre-war pacifism. Mrs Parks is not as mystical as Weil was. But her life has been an affirmation of Weil's conviction that readiness to die for your religious beliefs is not a conclusive sign of faith in God. To be willing to die for a victim of injustice, even a stranger—that, for Weil, was the truer test of religious faith.

Simone Weil
By Francine du Plessix Gray

Viking; 256 pages; $19.95. Weidenfeld & Nicolson; £12.99

Buy it at
Amazon.com
Amazon.co.uk

Mine Eyes Have Seen The Glory: The Life of Rosa Parks
By Douglas Brinkley

Viking; 160 pages; $19.95. Weidenfeld & Nicolson; £12.99

Buy it at
Amazon.com
Amazon.co.uk

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Daniel Ellsberg

Treachery, egotism or bravery?

Jul 19th 2001
From The Economist print edition

THIRTY years have passed, but Americans are still arguing about the significance of the publication in 1971 of the so-called Pentagon Papers, a top-secret history of American involvement in South-East Asia commissioned by Robert McNamara three years earlier, just as he was beginning to lose heart for the war he was fighting there on behalf of Lyndon Johnson. The death of Katharine Graham, the publisher of the *Washington Post* (see article), also vividly brings back those times. Together with its competitor, the *New York Times*, her newspaper won a famous free-speech victory in the Supreme Court after attempts to prevent the publication of the Vietnam study.

Wild Man: The Life and Times of Daniel Ellsberg
By Tom Wells

Palgrave; 704 pages; $32.50 and £22.50

Buy it at
Amazon.com
Amazon.co.uk

When articles based on the documents first appeared in the *New York Times* on a sleepy Sunday late in spring, hardly anyone seemed to notice. Those who did thought they would harm the reputation of past Democratic administrations far more than the Republicans then in command of the executive branch. But soon Henry Kissinger, who was then national-security adviser in the White House, persuaded Richard Nixon that such a massive leak of classified information (47 volumes, thousands of pages) could threaten the very security of the United States, and in particular compromise the secret diplomacy Mr Kissinger was then conducting with China. Mr Nixon, who was prepared to believe the most abstruse conspiracy theories, sent lawyers from his Justice Department into federal court to stop the presses and obtain a rare prior-restraint order against further publication of the confidential material.

What ensued during the following fortnight was part high drama, part vaudeville show. Government lawyers stumbled over themselves as they tried to make the best legal presentation they could of a wretched case. The leak of the documents spread to the *Washington Post*, the *Boston Globe* and other newspapers around the country. Judges held secret hearings and issued eloquent opinions rejecting Nixon's case. Finally, the Supreme Court ruled in the newspapers' favour and let the presses roll, albeit after a temporary episode of censorship.

Among the most intriguing figures to emerge during the episode was Daniel Ellsberg, a former gung-ho marine and war planner at the Rand Corporation who had turned against the American engagement in Vietnam. As one of the documents' authors, and after failing to persuade senators and statesmen to make them public, he handed them over to the *Times*. He was subsequently indicted and tried in Los Angeles under statutes punishing espionage and theft of government property; but the case was dismissed after it was revealed that White House "plumbers", in what turned out to be a dress rehearsal for their burglary of the Democratic National Committee's offices in the Watergate building, had broken into the office of Mr Ellsberg's psychiatrist, looking for files that might shed light on his dastardly deeds—or provide dirt against him.

In good time for 30th anniversary soul-searching and celebrations last month, along has come Tom Wells's full-scale but unauthorised biography of Mr Ellsberg, which is nearly as long as the Pentagon Papers themselves. It would appear that the author has been at work on this project for almost the entire time since the papers were published, interviewing everyone he could find who met Mr Ellsberg and quoting them all at interminable length, even if they repeated themselves.

Much of what Mr Wells found is interesting, some of it even fascinating. Other parts, alas, are drivel—facile pop psychologising and psychoanalysing by a person who brings no professional credentials to the task. Here is information on Mr Ellsberg's sex life, his often poor performance—or bad luck—as a parent, and his continuing debates with friends and adversaries alike over issues that simply cannot be resolved. What does emerge from Mr Wells's work, though, is a classic tale of a man whose life and reputation were totally redefined by a single act. To this day, people are arguing over whether that act was one of bravery, treachery, or mere egotism, and all sides can find support for their positions in this thoroughly under-edited volume.

Mr Ellsberg believed that release of the Pentagon Papers would (or certainly should) immediately stop the war in Vietnam. This did not happen, of course, although the information that became known through them—including evidence of cynicism and deception by every administration from Truman through Johnson—certainly made it more acceptable for politicians and pundits to speak against the doomed military effort.

Between appearances at public protests on other foreign policy, defence and social issues, Mr Ellsberg is still active on the lecture and conference circuit, demanding recognition, appreciation and understanding. Only one thing diverts him now: his effort to get the public to realise that Mr Wells, seemingly possessed of his own obsessions, has written an unbalanced and unfair biography.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

New fiction

Not amused

Jul 19th 2001
From The Economist print edition

DAVID CZUCHLEWSKI'S debut novel comes with a glowing endorsement from his former writing advisor, Joyce Carol Oates. She declares it "an ingeniously plotted postmodernist mystery". The "Muse Asylum" referred to in the book's title is a fancy upstate New York psychiatric hospital for "the artistically gifted mentally ill". Andrew Wallace, recently sent down from college, is a patient there. He's busy scribbling a memoir, most of which concerns a reclusive writer called Horace Jacob Little. Nobody has a clue what this man looks like, where he lives or whether he exists at all. But Andrew is convinced, on the evidence of a short story, that Horace Jacob Little is at the centre of all manner of dire plots and conspiracies.

The Muse Asylum
By David Czuchlewski

G.P. Putnam's Sons; 225 pages; $23.95
G.P. Putnam's Sons; 225 pages; $23.95

Buy it at
Amazon.com

Jake Burnett was a contemporary of Andrew's at college. These days he's a reporter on a small New York weekly. Looking for leads on a possible article about Horace Jacob Little, he heads up to the Muse Asylum to quiz Andrew. The story of Jake's hunt for Horace Jacob Little is interspersed with flashbacks to his college days and excerpts from Andrew's "Confessions". There's a romantic interest, too, in the comely form of Lara Knowles. After a fling with Jake she took up with Andrew while they were all still students. It turns out that Horace Jacob Little is living in central Manhattan, just a bagel's throw from Jake's office. By and by, and with a dramatic twist or two, the plot thickens.

Mr Czuchlewski doesn't wear his Eng. Lit. background lightly. There are nudge-nudge, wink-wink references to "the death of the author" and ruminations on madness and creativity. All of which would be easier to take if the writing itself were better. Awoken by a thunderclap in the middle of the night, Jake recalls: "I knew I would not be able to get back to sleep. I had broken through the threshold of night, beyond which sleep would not come—only a rapid stream of thoughts and disconnected suppositions." Now what would the great Horace Jacob Little make of a sentence like that?

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Immigration

No entry

Jul 19th 2001
From The Economist print edition

The costs and follies of keeping immigrants out

ALL history is the history of migrations. All of us got to where we are because we or our ancestors came from somewhere else. Migrants usually help host-communities, bringing new skills, new vigour, demographic infill and fresh ideas. They are vectors of change, which sometimes seems to threaten indigenous culture; but cultural change comes equally from within and you threaten in any event to stifle a society by excluding immigrants. It seems incredible that people who pride themselves on descent from Saxon and Norman and Dane should be unaware of the value of immigrants; or that zeal for barriers should thrive in a country so enriched in modern history by infusions, for instance, of Huguenots, Jews and black and Asian "counter-colonists" from the former empire. Opposition to immigration is historically ignorant. In contrasting ways, new books by Sir Michael Dummett and Teresa Hayter argue, with particular reference to Britain, that it is also irrational and immoral.

Ms Hayter devotes most of her book to a chilling narrative of racism, migrant-phobia and "creeping fascisisation" in modern Britain. Her case against controls, when she gets round to it, concentrates on seven points. Controls are expensive (though supporters might still say they are worthwhile). They are unnecessary, because the numbers of potential immigrants are small (probably true, but Ms Hayter does not deal with the powerful case to the contrary made, for example, by Paul Kennedy, author of "Preparing for the 21st Century"). They inhibit cultural diversity (true again, but, unfortunately, most British people seem grossly to undervalue cultural diversity). They create a class of illegal workers (but this seems a bonus from the perspective of employers who want an exploitable labour-pool). Emigrants are good for developing countries (but this could be construed as an argument in favour of multiplying the numbers of cheap "illegals"). Controls are incompatible with strictly economic liberalism (which looks like a strong point, but Ms Hayter is strangely reluctant to insist that free movement of labour and free trade are inseparable). Finally, immigration controls foment racism: this is an important point—since British governments always try to justify anti-immigrant measures "in the interests of good race relations"—and deserves more space than it gets.

Open Borders: The Case Against Immigration Controls
By Teresa Hayter

Stylus Publishing; 224 pages; $60 ($19.95 paperback). Pluto Press; £40 (Ã‚Â£12.99 paperback)

Buy it at
Amazon.com
Amazon.co.uk

On Immigration and Refugees
By Michael Dummett

Routledge; 174 pages; $12.95 and £7.99

Buy it at
Amazon.com
Amazon.co.uk

Peoples and Empires
By Anthony Pagden

Modern Library; 240 pages; $19.95. Weidenfeld & Nicolson; £12.99

Buy it at
Amazon.com
Amazon.co.uk

Sir Michael is a renowned philosopher and humanitarian, who explains his vocation in defence of refugees as "an accident" unrelated to his philosophical and religious convictions. In his new book, however, he seeks moral foundations for the case against immigration controls. His main arguments are, first, that the state has obligations which transcend the national interest and include a duty of humanity towards refugees; and, secondly, that the state has no right to exclude immigrants, except where the indigenous community is genuinely in danger of "submersion" by newcomers. He makes the case meticulously. His emphasis on duties rather than rights will broaden the appeal of his case. But he leaves unaddressed the most likely counter-argument: that a democratic state is a free association and freedom of association involves a right of exclusion.

The strongest part of his book, as of Ms Hayter's, is the account of the hypocrisy, faithlessness, demagogy, moral indifference and, at times, outright cruelty shown by different British governments on this issue since the 1960s. Like the "Analects" of Confucius, Sir Michael's narrative gains power from its cold-blooded, uncoloured language. Between them, he and Ms Hayter provide a terrible indictment of modern British immigration policy. Both writers are good at exposing the insidious rhetoric which turns refugees into "bogus asylum-seekers" and demonises "economic migrants", who, in reality, are often the

sort of go-ahead venturers capitalism needs. Governments seem keener to appeal to that ineradicable British vice, xenophobia, than to that ineradicable British virtue, a sense of fair play.

One context in which immigrants can justly be resisted is when they come bearing arms to establish an empire. Western imperialism has been responsible for some of the most conspicuous mass migrations of the last half-millennium: exporting elites, re-shuffling labour forces, transporting slaves and coolies and triggering the counter-colonisations of the last half-century, when former “victim” peoples have settled in the “mother-countries” of their sometime masters. Anthony Pagden’s distillation of the history of western empires is a triumph of *multum in parvo*. It is not, however, about migration itself, but about the political nature of imperialism. Mr Pagden unravels two intertwined threads: one leads from Alexander to the early-modern Spanish monarchy and King Leopold’s Congo; another from ancient Rome to the United States and the lately vanished empires of democratic nations. Empires are always tyrannous, but not always despotic. Some of them are of, by and for the people. The sad story of hostility to immigrants points to a similar conclusion: democracy is no guarantee of humanity—or good sense.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Correction

Jul 19th 2001
From The Economist print edition

Walter Rantanen, a paper-fibre microscopist, who was quoted in our article of July 7th on fake vintage photography, has at times analysed documents for the FBI, but he is not an FBI employee.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Katharine Graham

Jul 19th 2001
From The Economist print edition

Katharine Graham, who helped to topple a president, died on July 17th, aged 84

SHE liked to tell the story of a visit to a village in Côte d'Ivoire where the chief welcomed her by saying how honoured he was to be visited by the 17th most important person in the world. No doubt those who compose lists of the 100 most important people of the 20th century will quibble about exactly which position Katherine Graham should hold. But there is no doubt that she will make the list.

AP

Mrs Graham presided over the transformation of the *Washington Post* from a provincial newspaper that happened to be based in the nation's capital into a great American institution. In the process, she transformed herself from a shy blueblood into one of the most important power-brokers in the capital at the height of the American century. She guided the *Post* through two of the most celebrated episodes in American journalism.

One was the publication in 1971 of the "Pentagon Papers", a secret government history of the Vietnam war. The other was the Watergate scandal that broke in 1972, which led to Richard Nixon's resignation from the presidency two years later under the threat of impeachment. Somewhere along the way, Katharine Graham turned the *Post* into a great money-making machine. When she took control of the newspaper in 1963, the company had revenues of $84m; when she stepped down as chief executive in 1991 and handed over to her eldest son, it had revenues of $1.4 billion.

All this took enormous guts—"the guts of a burglar", in the words of Ben Bradlee, whom she plucked from *Newsweek* to act as the *Post*'s executive editor and her journalistic right hand throughout her career. Mrs Graham went ahead with the publication of the "Pentagon Papers", although an adverse legal ruling could have derailed the company's then imminent public offering of $35m in stock and jeopardised the company's licences for its two Florida television stations, then worth about $100m. She supported Carl Bernstein's and Bob Woodward's investigation of the Watergate saga despite a constant drumbeat of threats from the White House.

The antique wringer

In those days, a Wall Street friend with contacts in the administration advised Mrs Graham not to be alone. Nixon's campaign manager, John Mitchell, told Mr Bernstein that "Katie Graham's gonna get her tit caught in a wringer" if the *Post* printed a story that, while Mitchell was attorney-general, he shared control of a secret fund to gather intelligence on Democrats. A prized possession was an antique washing-machine wringer that Mr Woodward gave her when the nightmare was over.

Mrs Graham showed the same guts when it came to taking on the printers' union in 1975-76—what she referred to as her "business-side Watergate". She had supported vaguely leftist causes at university. But she refused to yield to the printers' unions when they tried to use violence and intimidation to preserve old practices. She showed no compunction about using replacement workers.

"It's sort of like a fairy tale," Mrs Graham said on being told that she was being awarded a Pulitzer prize for her autobiography, "Personal History". In fact, her life was beguiling because of the misfortunes she coped with. The daughter of a rich Wall Streeter, Eugene Meyer, she happily embraced her destiny of raising children and hosting dinner parties when she finally met the charming and charismatic Philip

Graham, whom Meyer made publisher of the *Post*. But Philip turned out to be mentally unbalanced, and drifted in and out of mental institutions before putting a gun to his head.

Her husband's death forced Mrs Graham to transform herself into a businesswoman—and, in the process, to kick against conventional assumptions about women's role in the world. She was brought up to think that the role of women was to look after their husbands. Now she was boss of the *Post*.

All this meant that Katharine Graham was painfully badly prepared for corporate politics. She was embarrassed about speaking to her own reporters, let alone about challenging the paper's executives. She was so ill at ease that she spent some time rehearsing how to say "Merry Christmas" before attending her first company Christmas party as boss. Warren Buffett, her financial mentor, recalls walking into her office to find a sheet of paper on her desk that read "assets on the left, liabilities on the right". And that was ten years after she had taken over.

But Mrs Graham discovered to her surprise that she had been born with a spine of steel. In giving the toast at her 70th birthday, Art Buchwald said, "There is one word that brings us all together here tonight. And that word is 'fear' ." Even more important, she also discovered that she had been born with a moral compass.

It wasn't fear that filled the *Post* on the day after her death with obviously heartfelt encomiums from senior journalists. It was genuine admiration for her sense of principle. During Watergate, Mrs Graham backed her journalists against the advice of her lawyers and accountants for the simple reason that she thought the principle raised by Richard Nixon's "third-rate break-in" was more important than mere cashflow. Journalists cannot ask for more from a proprietor than that.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Money and interest rates

Jul 19th 2001
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jul 18th 2001)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+13.1	+ 6.9	May	5.05	6.22	5.41	6.03	6.26	7.58
Britain	+ 6.7	+ 7.4	May	5.19	6.09	5.30	5.09	5.20	6.46
Canada	+12.7	+ 6.2	May	4.12	5.64	4.73	5.74	5.98	7.33
Denmark	+ 1.2	- 6.9	May	4.93	5.77	4.75	5.23	5.71	7.15
Japan	+ 8.1	+ 3.2	Jun	0.01	0.11	0.05	1.35	1.68	1.50
Sweden	+ 5.9	- 1.4	May	4.30	4.04	4.79	5.35	5.30	5.67
Switzerland	nil	+ 3.6	Jun	3.23	3.46	3.35	3.38	3.84	4.17
United States	+ 1.6	+11.3	Jun	3.59	6.53	3.92	5.09	6.57	6.98
Euro area†	+ 3.5	+ 5.4	May	4.48	4.84	4.28	4.94	5.24	5.63

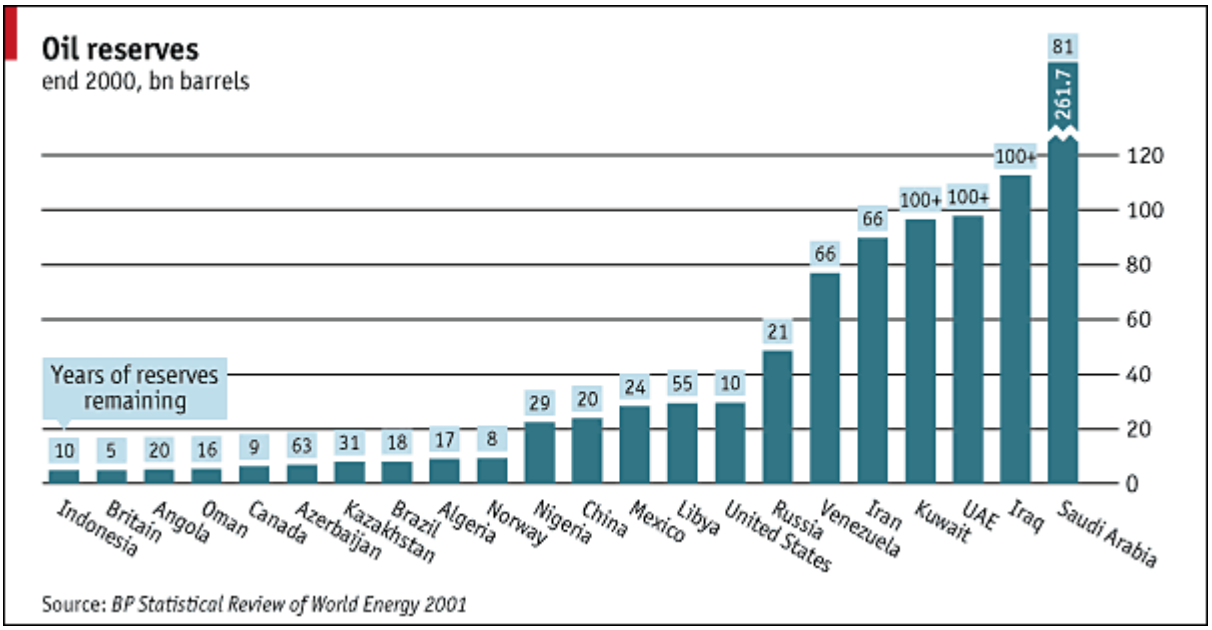
*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 5.52%, Japan No.232 1.37%. Central bank rates: US fed funds 3.75%, ECB refinancing 4.50%, BOJ overnight call 0.01%, BOE repo 5.25%.
Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, OM Fixed Income Exchange, Warburg Dillon Read, DRI-WEFA, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Oil reserves

Jul 19th 2001
From The Economist print edition

Saudi Arabia remains the kingpin of oil. It has a quarter of the world's proven reserves, about 262 billion barrels of oil, under its vast desert expanses. Add in the reserves held by the country's allies in the OPEC cartel, and the total is a whopping 815 billion barrels—some three-quarters of world reserves. In contrast, OECD countries, which use much of the world's oil, have less than one-tenth of total reserves.



Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Commodity price index

Jul 19th 2001
From The Economist print edition

1995=100

	Jul 10th	Jul 17th*	% change on one month	% change on one year
Dollar index				
All items	69.0	70.4	+ 1.4	- 3.9
Food	68.8	71.3	+ 5.1	- 0.5
Industrials				
All	69.2	69.1	- 3.4	- 8.4
Nfa†	68.3	68.4	- 3.1	+ 0.5
Metals	70.0	69.8	- 3.7	-14.6
Sterling index				
All items	77.1	79.3	+ 1.5	+ 2.6
Euro index				
All items	106.0	108.7	+ 2.1	+ 5.2
Yen index				
All items	92.1	93.7	+ 3.2	+11.1
Gold				
$ per oz	267.40	267.95	- 2.4	- 5.3
West Texas Intermediate				
$ per barrel	27.26	25.28	- 7.5	-20.6

* Provisional. † Non-food agriculturals.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Stockmarkets

Jul 19th 2001
From The Economist print edition

Market indices

	Jul 18th	2001 high	2001 low	% change on one week	% change on record high	% change on Dec 31st 2000 in local currency	% change on Dec 31st 2000 in $ terms
Australia (All Ordinaries)	3,339.6	3,425.2	3,094.3	+ 0.5	- 2.5	+ 5.9	- 2.0
Austria (ATX)	1,216.2	1,244.9	1,052.2	+ 0.3	- 30.0	+ 13.3	+ 5.2
Belgium (Bel 20)	2,948.5	3,030.4	2,591.6	+ 2.7	- 19.9	- 2.5	- 9.5
Britain (FTSE 100)	5,404.6	6,334.5	5,314.8	+ 0.2	- 22.0	- 13.1	- 17.7
Canada (Toronto Composite)	7,620.5	9,348.4	7,415.5	+ 0.7	- 33.1	- 14.7	- 16.5
Denmark (KBX)	254.7**	294.3	234.7	- 2.5	- 15.6	- 3.8	- 10.5
France (SBF 250)	3,143.3	3,820.2	3,107.9	- 0.8	- 28.4	- 16.7	- 22.6
(CAC 40)	4,867.5	5,998.5	4,824.8	- 1.0	- 29.7	- 17.9	- 23.8
Germany (Xetra DAX)	5,728.4	6,795.1	5,388.0	- 1.3	- 29.0	- 11.0	- 17.4
Italy (BCI)	1,555.8	1,948.4	1,578.6	- 2.7	- 28.7	- 18.8	- 24.7
Japan (Nikkei 225)	11,892.6	14,529.4	11,819.7	- 0.9	- 69.4	- 13.7	- 20.8
(Topix)	1,199.7	1,441.0	1,162.0	- 2.3	- 58.4	- 6.5	- 14.2
Netherlands (AEX)	539.4	642.3	518.3	- 2.2	- 23.1	- 15.4	- 21.5
Spain (Madrid SE)	803.9	963.9	798.6	- 0.4	- 29.9	- 8.7	- 15.3
Sweden (Affarsvarlden Gen)	221.7	293.1	217.2	- 0.5	- 44.6	- 20.2	- 29.0
Switzerland (Swiss Market)	6,857.6	8,135.4	6,574.0	+ 0.7	- 18.5	- 15.7	- 21.0
United States (DJIA)	10,569.8	11,337.9	9,389.5	+ 3.2	- 9.8	- 2.0	- 2.0
(S&P 500)	1,207.7	1,373.7	1,103.3	+ 2.3	- 20.9	- 8.5	- 8.5
(Nasdaq Comp)	2,016.2	2,859.2	1,638.8	+ 2.2	- 60.1	- 18.4	- 18.4
Europe (FTSE Eurotop 300)*	1,307.5	1,545.5	1,279.0	- 0.7	- 23.3	- 14.7	- 20.9
Euro area (FTSE Ebloc 100)*	1,155.9	1,404.1	1,143.9	- 1.3	- 25.5	- 17.0	- 22.9
World (MSCI)†	1,058.8	1,249.2	1,014.6	+ 1.3	- 26.9	na	- 13.3
World bond market (Salomon)‡	431.6	447.8	420.6	+ 0.7	- 6.2	na	- 2.8

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in dollar terms. **New index.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

PRINTABLE PAGE VIEW SPONSORED BY

About sponsorship

Trade, exchange rates and budgets

Jul 19th 2001
From The Economist print edition

	Trade balance*, $bn latest 12 months	Current account $bn latest 12 mths	Current account The Economist poll % of GDP, forecast 2001	Current account The Economist poll % of GDP, forecast 2002	Exchange rate trade-weighted† Jul 18th	Exchange rate trade-weighted† year ago	Currency units per $ Jul 18th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2001‡
Australia	− 1.4 May	− 12.9 01	− 3.0	− 3.0	72.9	76.0	1.94	1.73	2.75	1.69	1.56	0.1
Austria	− 5.6 Apr	− 4.5 Apr	− 2.2	− 2.0	100.0	99.9	15.8	14.9	22.4	13.8	12.7	-0.6
Belgium	+ 12.1 May	+ 11.2 Mar	+ 4.2	+ 4.5	98.6	98.7	46.3	43.6	65.5	40.3	37.2	0.7
Britain	− 44.0 May	− 19.2 01	− 2.1	− 2.4	106.3	105.9	0.71	0.67	-	0.67	0.57	1.2
Canada	+ 45.8 Apr	+ 22.2 01	+ 3.3	+ 2.6	78.6	80.6	1.54	1.47	2.17	1.34	1.23	2.6
Denmark	+ 6.1 Apr	+ 4.3 May	+ 1.6	+ 1.7	101.7	100.6	8.55	8.06	12.1	7.45	6.87	2.9
France	− 0.2 May	+ 14.0 May	+ 1.7	+ 1.8	101.1	101.4	7.53	7.10	10.7	6.56	6.05	-0.5
Germany	+ 57.4 May	− 17.4 May	− 0.8	− 0.6	98.1	98.0	2.24	2.12	3.18	1.96	1.80	-1.7
Italy	+ 2.2 Apr	− 6.1 Apr	− 0.3	− 0.1	72.2	72.3	2,222	2,095	3,146	1,936	1,787	-1.3
Japan	+ 95.6 May	+102.3 May	+ 2.2	+ 2.0	136.9	153.0	124	108	176	108	-	-6.3
Netherlands	+ 17.3 Apr	+ 16.0 01	+ 4.1	+ 4.0	97.4	97.5	2.53	2.38	3.58	2.20	2.03	1.3
Spain	− 38.9 Apr	− 15.9 Apr	− 2.8	− 2.7	73.9	74.0	191	180	270	166	154	nil
Sweden	+ 12.9 May	+ 5.7 May	+ 2.1	+ 2.3	75.2	83.3	10.61	9.07	15.0	9.24	8.53	3.6
Switzerland	− 0.1 May	+ 28.3 01	+11.5	+11.5	109.0	105.9	1.73	1.68	2.45	1.51	1.39	na
United States	−458.2 Apr	−449.3 01	− 4.1	− 3.9	120.3	111.1	–	–	1.42	0.87	0.80	2.1
Euro area	− 6.8 Apr	− 30.0 Apr	− 0.3	− 0.1	77.7	78.9	1.15	1.08	1.67	-	0.92	-0.6
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*												
Finland	+ 14.0 May	+ 8.9 May	na	na	77.8	76.8	6.91	6.43	9.78	6.02	5.56	5.3
Greece	− 7.5 Jan	− 7.7 Jan	na	na	57.2	57.9	396	364	561	345	319	nil
Iceland	− 0.4 May	− 0.9 04	na	na	na	na	103	79.6	146	89.7	82.8	2.4
Ireland	+ 27.9 Apr	− 1.3 01	na	na	86.7	87.0	0.92	0.85	1.30	0.80	0.74	4.5
Luxembourg	− 2.4 Apr	+ 1.2 01	na	na	98.6	98.7	46.9	43.6	66.4	40.9	37.7	3.6
New Zealand	− 0.1 May	− 2.3 01	na	na	79.1	80.8	2.41	2.20	3.41	2.10	1.94	1.0
Norway	+ 27.8 Jun	+ 25.6 Apr	na	na	95.2	91.9	9.19	8.85	13.0	8.01	7.39	15.3
Portugal	− 13.9 Apr	− 9.9 Apr	na	na	89.0	89.0	233	217	330	203	187	-1.2

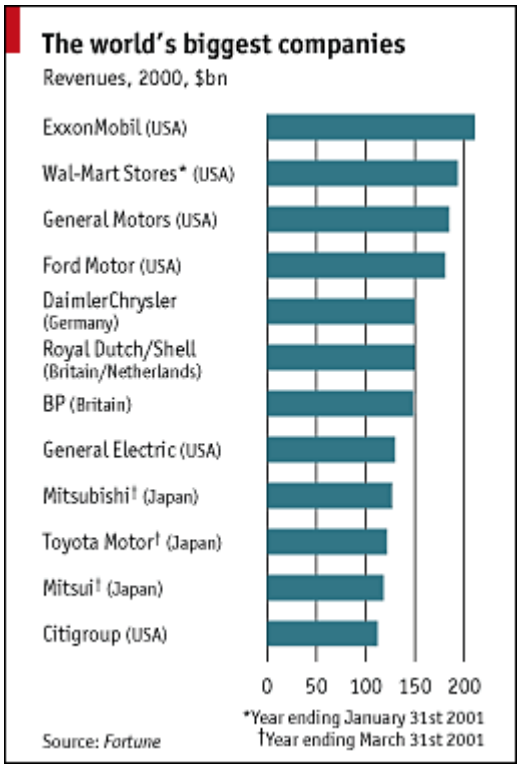
*Merchandise, Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others oil/fob. †1980=100, Bank of England. ‡OECD estimate.

† extrefers only to the first 16 countries listed

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The world's biggest companies

Jul 19th 2001
From The Economist print edition



Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Overview

Jul 19th 2001
From The Economist print edition

America's economy is still ailing. Industrial production shrank by 0.7% in June, the ninth straight month of decline. That makes this the longest period of contraction since 1982. Capacity utilisation fell to 77% in June, the lowest since August 1983. Meanwhile, inflation was slightly higher than expected: the consumer-price index (CPI) rose by 0.2% in June, to give a 12-month increase of 3.2%. The core CPI, which excludes food and energy prices, rose by 0.3% in June, compared with 0.1% in May.

The Dow Jones Industrial Average rose by 3.2%; but the **dollar** fell to a two-month low against the euro.

Inflation dipped in the **euro area**. Consumer prices rose by 3.0% in the 12 months to June, down from 3.4% in May. Excluding energy, food, alcohol and tobacco, however, inflation was unchanged in June at 2.1%.

France's external account deteriorated sharply. The 12-month visible-trade balance swung into a $150m deficit in May, compared with a surplus last year of $12.1 billion. The current-account surplus shrank to $14.0 billion in the same period, less than half its level a year ago. Industrial output was stronger than expected, however, rising by 0.3% in May after a 0.4% fall in April.

In **Britain**, unemployment reached a record low; but growth in wages slowed. As measured by the Labour Force Survey, preferred by the government, unemployment fell to 4.9% in the three months to May. That is the lowest since the series began in 1984. The year-on-year growth in wages slowed to 4.5% in the three months to May.

Japan's economic condition seems to be deteriorating. The ESRI's Economy Watchers survey of current conditions fell to 38.2 in June from 42.3 a month before, the lowest since the survey began last year. The decline in the outlook for the next two to three months was even greater: the figure fell from 48.4 in May to 42.3 in June. Japan's Topix stockmarket index fell by 2.3%.

Oil futures in New York sank to a 14-month low on July 18th. The August contract fell for the eighth day running, touching $24.60 a barrel, after America's Energy Information Administration (EIA) reported that American stocks of crude oil had soared by 7m barrels to 315m barrels.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Output, demand and jobs

Jul 19th 2001
From The Economist print edition

% change at annual rate

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr	1 year	2001	2002	1 year	1 year	latest	year ago
Australia	+ 4.3	+ 2.1 Q1	+ 2.3	+ 3.8	+ 3.1 Q4*	+ 3.0 Q1	6.9 Jun	6.3
Austria	+ 1.6	+ 2.2 Q1	+ 2.0	+ 2.3	+ 2.5 Apr	+ 2.6 Mar	3.7 May	3.7
Belgium	+ 1.8	+ 2.4 Q1	+ 2.3	+ 2.6	– 2.9 May*	– 1.7 Apr	9.9 Jun*	10.1
Britain	+ 1.7	+ 2.7 Q1	+ 2.2	+ 2.8	– 1.9 May	+ 6.4 May	4.9 May‡	5.6
Canada	+ 2.5	+ 2.6 Q1†	+ 2.3	+ 3.1	+ 1.0 Apr	+ 3.0 Mar	7.0 Jun	6.6
Denmark	– 4.6	+ 1.0 Q1	+ 1.5	+ 2.1	+ 1.7 Apr	+ 0.2 Apr	5.2 May	5.4
France	+ 2.0	+ 2.7 Q1	+ 2.2	+ 2.5	+ 1.9 May	– 2.5 May	8.7 May	9.6
Germany	+ 1.5	+ 1.6 Q1	+ 1.3	+ 2.1	– 1.8 May	– 2.3 May	9.3 Jun	9.6
Italy	+ 2.8	+ 2.4 Q1	+ 2.0	+ 2.3	– 1.9 May	– 0.8 Apr	9.6 Apr	10.7
Japan	– 0.8	– 0.1 Q1	– 0.3	+ 0.9	– 3.9 May	+ 0.1 Apr	4.9 May	4.6
Netherlands	+ 0.2	+ 2.0 Q1	+ 2.2	+ 2.9	– 2.0 May	+ 1.5 Mar	1.8 Jun§	2.7
Spain	+ 4.1	+ 3.3 Q1	+ 2.7	+ 2.9	– 0.4 May	na	12.9 May	14.3
Sweden	+ 2.4	+ 2.3 Q1	+ 2.3	+ 2.8	– 1.4 Apr	+ 2.3 Apr	3.5 May*	4.1
Switzerland	+ 7.4	+ 2.5 Q1	+ 1.8	+ 2.1	+ 5.1 Q1*	– 0.7 May	1.6 Jun*	1.8
United States	+ 1.2	+ 2.5 Q1	+ 1.6	+ 2.9	– 3.6 Jun	+ 2.5 Apr	4.5 Jun	4.0
Euro area	+ 2.0	+ 2.6 Q1	+ 1.9	+ 2.4	+ 1.6 Apr	+ 1.5 Apr	8.3 May	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	– 0.4	+ 3.4 Q1	na	na	– 2.3 May	+ 6.9 Mar	11.3 May*	11.9
Greece	na	+ 2.52000	na	na	– 0.8 Mar*	+ 5.1 Mar	na	na
Iceland	na	+ 3.62000	na	na	+ 2.5 2000	na	1.5 Apr	1.5
Ireland	na	+12.1 Q4	na	na	+17.0 Apr*	+ 1.6 Mar	3.7 Jun	4.1
Luxembourg	na	+ 8.52000	na	na	+ 8.6 Mar*†	+ 6.7 Mar	2.4 May	2.7
New Zealand	+ 0.9	+ 0.4 Q1	na	na	+ 0.9 Q1*	+ 1.7 Q1	5.4 Q1	6.4
Norway	+ 0.9	+ 0.3 Q1	na	na	– 5.9 May*	– 1.8 May	3.7 Q1	3.9
Portugal	+ 2.2	+ 3.4 Q4	na	na	+ 3.4 May*	+ 5.3 Mar	4.2 Q1	4.4

*Not seasonally adjusted. †New series. ‡Mar-May; claimant count rate 3.2% in Jun. §Apr-Jun

Text refers only to the first 16 countries listed

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Prices and wages

Jul 19th 2001
From The Economist print edition

% change at annual rate

	Consumer prices* 1 year		Consumer prices* year ago	The Economist poll consumer prices forecast 2001	The Economist poll consumer prices forecast 2002	Producer prices* 1 year		Producer prices* year ago	Wages/earnings 1 year		Wages/earnings year ago
Australia	+ 6.0	Q1	+ 2.8	+ 4.0	+ 2.4	+ 5.2	Q1	+ 5.6	+ 5.6	Q1	+ 2.9
Austria	+ 2.8	Jun	+ 2.7	+ 2.3	+ 1.7	+ 2.9	Jun	+ 3.8	+ 2.7	May	+ 1.9
Belgium	+ 2.9	Jun	+ 2.8	+ 2.4	+ 1.9	+ 5.3	May	+ 8.6	+ 1.9	Q1	+ 3.3
Britain	+ 1.9	Jun	+ 3.3	+ 2.1	+ 2.4	+ 0.4	Jun	+ 2.8	+ 4.5	May	+ 4.6
Canada	+ 3.9	May	+ 2.4	+ 2.8	+ 2.1	+ 2.7	May	+ 5.9	+ 0.9	Apr	+ 3.1
Denmark	+ 2.3	Jun	+ 3.3	+ 2.4	+ 2.2	+ 3.2	Jun	+ 6.6	+ 3.8	Q1	+ 3.6
France	+ 2.1	Jun	+ 1.7	+ 1.8	+ 1.5	+ 2.8	May	+ 5.8	+ 4.3	Q1	+ 5.2
Germany	+ 3.1	Jun	+ 1.9	+ 2.7	+ 1.7	+ 3.1	Jun	+ 5.4	+ 1.4	Apr*	+ 2.3
Italy	+ 3.0	Jun	+ 2.7	+ 2.7	+ 2.1	+ 2.9	May	+ 6.4	+ 2.7	May*	+ 2.3
Japan	– 0.5	May	– 0.7	– 0.4	– 0.3	+ 0.8	Jun	– 0.6	nil	May	+ 2.1
Netherlands	+ 4.5	Jun	+ 2.7	+ 4.6	+ 2.7	+ 4.4	May	+ 8.2	+ 3.9	May	+ 3.3
Spain	+ 4.2	Jun	+ 3.4	+ 3.7	+ 2.8	+ 2.7	May	+ 5.8	+ 2.2	Q4	+ 2.4
Sweden	+ 2.9	Jun	+ 1.2	+ 2.2	+ 1.8	+ 2.6	May	+ 3.7	+ 1.8	Apr*	+ 4.1
Switzerland	+ 1.6	Jun	+ 1.8	+ 1.3	+ 1.3	+ 0.4	Jun	+ 2.9	+ 1.3	2000	+ 0.3
United States	+ 3.2	Jun	+ 3.7	+ 3.2	+ 2.3	+ 2.5	Jun	+ 4.4	+ 4.2	Jun	+ 3.7
Euro area	+ 3.0	Jun	+ 2.4	+ 2.7	+ 1.9	+ 3.6	May	+ 5.3	+ 2.6	Q1	+ 2.4
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 3.0	Jun	+ 3.5	na	na	+ 2.4	Jun	+ 8.6	+ 5.0	Q1*	+ 3.5
Greece	+ 3.9	Jun	+ 2.5	na	na	+ 5.1	Apr	+ 7.0	na		na
Iceland	+ 6.8	Jun	+ 5.5	na	na	+ 5.9	Jun	+ 3.9	+ 8.0	May	+ 7.1
Ireland	+ 5.3	Jun	+ 5.5	na	na	+ 2.4	May	+ 5.9	+ 6.4	Q4*	+ 7.3
Luxembourg	+ 2.9	Jun	+ 3.3	na	na	+ 2.5	Apr	+ 5.5	+ 7.2	Mar*	+ 4.2
New Zealand	+ 3.2	Q2	+ 2.0	na	na	+ 7.8	Q1	+ 4.9	+ 1.8	Q1	+ 1.4
Norway	+ 3.8	Jun	+ 3.3	na	na	+ 3.5	Jun	+ 8.3	+ 4.4	Q1*	+ 4.1
Portugal	+ 4.5	Jun	+ 2.9	na	na	+ 5.6	May	+14.9	+ 2.4	Apr*	na

*Not seasonally adjusted.

Text refers only to the first 16 countries listed

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

The Economist poll of forecasters

Jul 19th 2001
From The Economist print edition

Every three months *The Economist* polls a group of forecasters and calculates the average of their predictions for growth and current-account balances for 25 emerging economies. Since our poll in April, the panel has cut its growth forecasts for 2001 everywhere except China, which is still expected to grow by 7.5%. The biggest revision has been in Turkey, where GDP is now expected to contract by 4.8% this year. Argentina, another troubled debtor, is tipped to grow by only 0.4%. Singapore's growth has been slashed to 2.4%, down from a forecast of 6.2% only last October.

July

	Real GDP % change		Current account % of GDP	
	2001	2002	2001	2002
China	7.5	7.7	0.9	0.5
Hong Kong	2.5	4.4	3.6	2.2
India	5.8	6.3	–0.8	–0.7
Indonesia	2.8	3.9	2.7	1.7
Malaysia	3.0	5.1	6.3	4.6
Philippines	2.1	3.4	9.3	8.0
Singapore	2.4	5.5	21.4	20.0
South Korea	3.3	5.2	2.8	2.0
Taiwan	2.3	4.9	3.5	3.3
Thailand	2.5	4.0	4.7	3.3
Argentina	0.4	3.0	–3.2	–3.4
Brazil	2.5	3.5	–4.1	–4.0
Chile	3.8	4.9	–2.2	–2.6
Colombia	2.8	3.6	–1.7	–2.5
Mexico	1.7	4.3	–3.6	–3.8
Peru	0.6	4.0	–2.9	–2.4
Venezuela	3.4	3.1	4.7	2.9
Egypt	4.4	5.1	–0.5	–1.3
Israel	2.4	4.1	–2.6	–2.3
South Africa	2.9	3.3	–0.6	–1.0
Turkey	–4.8	4.5	1.7	–0.1
Czech Republic	3.4	3.9	–5.8	–5.8
Hungary	4.6	4.9	–4.4	–4.8
Poland	2.7	4.0	–4.9	–5.0
Russia	3.7	3.5	11.8	6.5

Sources: ABN Amro; Deutsche Bank; Economist Intelligence Unit; Goldman Sachs; HSBC; ING Barings; J.P.Morgan Chase; Merrill Lynch; Salomon Smith Barney; UBS Warburg.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Overview

Jul 19th 2001
From The Economist print edition

China's GDP grew by 7.8% in the year to the second quarter; industrial production was up by 10.1% in June from a year ago. Inflation fell to 1.4% in the same month.

The **Taiwanese** stockmarket tumbled by 7.2% to an eight-year low, as investors fretted about the depressed economy.

Turkey's industrial production fell by 9.7% in the year to May; **Malaysia**'s fell by 3.7% and **Mexico**'s fell by 3.4%.

Poland's inflation rate slowed to 6.2% in the year to June; **South Africa**'s slowed to 6.3%, **Israel**'s stayed at 0.7%, and **Malaysia**'s fell to 1.5%.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Economy

Jul 19th 2001
From The Economist print edition

	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 7.8	Q2	+10.1	Jun	+ 1.4	Jun	+19.9	Jun	+20.5	2000	180.2	Apr
Hong Kong	+ 2.5	Q1	– 0.1	Q1	– 1.5	May	–11.9	May	+ 8.8	Q1	114.1	Jun
India	+ 5.7	Q3	+ 1.9	May	+ 2.5	May	– 5.4	May	– 5.4	Q4	40.1	May
Indonesia	+ 4.0	Q1	+ 4.5	Q4	+12.1	Jun	+25.7	May	+ 5.5	Q3	22.1	Apr
Malaysia	+ 3.2	Q1	– 3.7	May	+ 1.5	Jun	+15.7	May	+ 8.4	Q4	25.6	May
Philippines	+ 2.5	Q1	+12.7	Apr	+ 6.7	Jun	+ 6.1	May	+ 9.1	Mar	12.5	Apr
Singapore	– 0.8	Q2	–10.9	May	+ 1.9	May	+ 7.7	Jun	+21.8	Q1	76.7	Apr
South Korea	+ 3.7	Q1	+ 2.3	May	+ 5.2	Jun	+14.3	Jun	+14.6	May	94.3	Jun
Taiwan	+ 1.1	Q1	– 8.2	May	– 0.2	Jun	+12.2	Jun	+12.0	Q1	110.6	May
Thailand	+ 1.8	Q1	+ 1.6	May	+ 2.3	Jun	+ 2.8	May	+ 6.6	May	31.4	May
Argentina	– 2.1	Q1	– 2.9	Jun	– 0.3	Jun	+ 1.7	May	– 9.0	Q1	20.2	May
Brazil	+ 4.1	Q1	+ 4.2	May	+ 8.1	Jun	– 1.6	Jun	–27.1	May	35.5	May
Chile	+ 3.3	Q1	+ 3.2	May	+ 3.6	Jun	+ 1.5	May	– 1.4	Q1	14.4	May
Colombia	+ 1.7	Q1	+ 2.2	May	+ 7.9	Jun	+ 1.6	Apr	– 0.7	Q1	9.7	May
Mexico	+ 1.9	Q1	– 3.4	May	+ 6.6	Jun	– 9.7	May	–17.8	Q1	40.6	May
Peru	– 0.4	May	+ 1.3	May	+ 2.5	Jun	– 0.3	May	– 1.7	Q4	8.3	May
Venezuela	+ 3.5	Q1	na		+12.5	Jun	+17.2	Dec	+12.5	Q1	10.9	May
Egypt	+ 6.5	2000†	+ 9.4	2000†	+ 2.2	May	–10.4	Q4	– 0.8	Q4	12.9	Mar
Israel	+ 1.8	Q1	+ 0.3	Apr	+ 0.7	Jun	– 7.5	Jun	– 1.4	Q4	23.2	May
South Africa	+ 2.7	Q1	+ 1.7	May	+ 6.3	Jun	+ 3.8	May	+ 0.1	Q1	6.1	May
Turkey	– 1.9	Q1	– 9.7	May	+56.1	Jun	–24.6	Apr	– 6.6	Apr	19.9	May
Czech Republic	+ 3.8	Q1	+ 6.9	May	+ 5.5	Jun	– 3.6	May	– 2.7	Q1	12.6	May
Hungary	+ 4.4	Q1	+ 8.4	May	+10.5	Jun	– 2.4	May	– 1.8	May	11.5	Jun
Poland	+ 2.3	Q1	– 1.0	May	+ 6.2	Jun	–10.2	May	– 9.0	May	26.9	Apr
Russia	+ 4.9	Q1	+ 3.7	May	+23.7	Jun	+59.7	May	+45.9	Q1	29.8	May
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 5.6	2000†	–12.9	Dec	+ 3.9	Apr	– 1.7	May	– 1.4	1999	1.2	Apr
Saudi Arabia	– 0.8	1999	na		+ 0.1	Apr	+24.9	1999	+ 0.4	1999	16.9	Mar

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Text refers only to the first 25 countries listed

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.

Financial markets

Jul 19th 2001
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jul 18th		Dec 31st 2000	
	Jul 18th	year ago	Jul 18th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	11.7	na	2,236.3	-1.0	+2.0	+2.0
Hong Kong	7.80	7.80	11.0	3.70	12,427.2	-0.8	-17.7	-17.7
India	47.2	44.8	66.8	7.04	3,383.4	+0.2	-14.8	-15.7
Indonesia	11,275	8,980	15,960	17.23	453.3	+3.6	+8.9	-6.6
Malaysia	3.80	3.80	5.38	3.30	647.7	+4.8	-4.7	-4.7
Philippines	54.3	44.5	76.9	10.56	1,393.2	+0.2	-6.8	-14.2
Singapore	1.83	1.75	2.59	2.31	1,627.8	-2.0	-15.5	-20.0
South Korea	1,307	1,112	1,850	5.33	540.5	-2.4	+7.1	+3.7
Taiwan	35.0	31.0	49.5	3.90	4,219.9	-7.2	-11.0	-15.8
Thailand	45.8	40.1	64.8	3.25	315.2	+0.8	+17.1	+11.0
Argentina	1.00	1.00	1.42	26.01	325.3	-4.2	-22.0	-22.1
Brazil	2.46	1.80	3.48	18.30	13,790.9	-0.2	-11.6	-29.9
Chile	655	548	927	3.57**	5,351.3	-1.2	+9.9	-3.7
Colombia	2,298	2,156	3,253	12.66	1,010.2	-0.4	na	na
Mexico	9.13	9.41	12.9	9.73	6,388.3	-2.7	+13.0	+19.0
Peru	3.50	3.48	4.9	8.26	1,314.8	-0.3	+8.8	+9.8
Venezuela	724	686	1,024	17.23	7,501.0	+0.6	+10.4	+6.8
Egypt	3.95	3.48	5.59	9.04	5,631.2	-7.3	-26.5	-27.6
Israel	4.21	4.10	5.96	4.68	421.6	+1.4	-14.8	-18.2
South Africa	8.21	6.98	11.6	9.78	8,704.3	-2.0	+4.5	-3.6
Turkey	1,369,500	632,825	1,938,527	66.00	9,105.9	+4.3	-3.5	-52.8
Czech Republic	38.9	38.6	55.1	5.29	382.3	-3.8	-20.1	-22.7
Hungary	285	281	404	11.18	6,573.3	+0.2	-16.3	-17.2
Poland	4.21	4.35	5.95	16.12	13,458.9	+2.9	-24.6	-25.9
Russia	29.3	27.7	41.4	25.00	195.4†	-0.4	+39.2	+36.4
EMF (MSCI)‡	1.00	1.00	1.42	na	297.4	-1.2	na	-10.9
EMBI+§	1.00	1.00	1.42	na	198.6	-1.7	na	-1.6

**Inflation adj. †In $ terms. ‡Emerging Markets Free. §J.P. Morgan Chase's Emerging Markets Bond Index Plus.

Copyright © 2006 The Economist Newspaper and The Economist Group. All rights reserved.